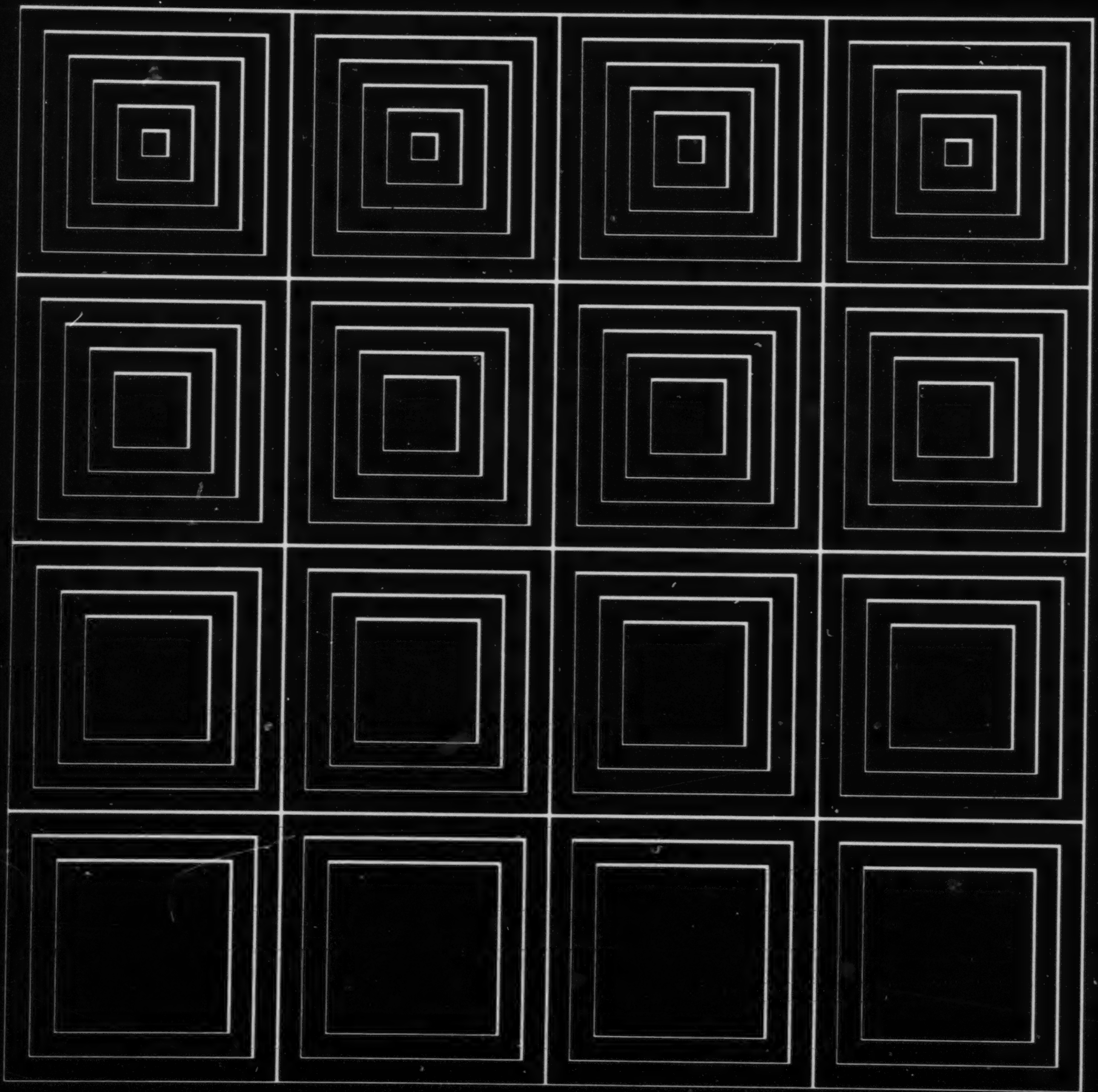
Report of the

Auditor General of Canada

to the House of Commons



Fiscal Year Ended 31 March 1989

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AUDITOR GENERAL OF CANADA
VÉRIFICATEUR GÉNÉRAL DU CANADA

To The Honourable the Speaker of the House of Commons:

I have the honour to transmit herewith my Report to the House of Commons for the fiscal year ended 31 March 1989, to be laid before the House in accordance with the provisions of section 7(3) of the Auditor General Act.

Kenneth M. Dye, F.C.A.
Auditor General of Canada

OTTAWA, 24 October 1989

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REPORT OF THE AUDITOR GENERAL TO THE HOUSE OF COMMONS FOR THE FISCAL YEAR ENDED 31 MARCH 1989

Introduction

REPORT OF THE AUDITOR GENERAL TO THE HOUSE OF COMMONS FOR THE FISCAL YEAR ENDED 31 MARCH 1989

Introduction

The principal functions and responsibilities of the Auditor General of Canada are set out in the Auditor General Act. My responsibilities in respect to those Crown corporations for which I have been appointed auditor are set out in the Financial Administration Act. The Auditor General Act is included as Appendix A to this report and the relevant sections of the Financial Administration Act as Appendix B.

The financial statements of the Government of Canada for the fiscal year ended 31 March 1989, which have been prepared by the Receiver General for Canada in accordance with the provisions of section 64 of the Financial Administration Act and appear in Volume I of the Public Accounts of Canada, have been examined by me as required by section 6 of the Auditor General Act.

In compliance with section 7 of the Auditor General Act, my report for the fiscal year ended 31 March 1989 is presented herewith.

As auditor of the accounts of Canada, including those relating to the Consolidated Revenue Fund, I conducted such examinations and inquiries as I considered necessary to enable me to report as required by the Auditor General Act.

With the exception noted below -- which is further discussed in Chapter 1 and Chapter 6 -- departments, agencies, and the Privy Council Office provided my Office with the information and explanations required to date, including Cabinet documents

The Supreme Court ruled on 10 August 1989 that in the event of a denial of access to information required by the Auditor General to fulfil his audit responsibilities, the ultimate remedy provided in the Auditor General Act is to report to the House of Commons. I am therefore again reporting that I have not received the information needed to complete the audit of the government's expenditures related to the acquisition of Petrofina Canada Inc.

In 1989-90 I planned to conduct a government-wide audit of expenses claimed by ministers for government travel and their use of Administrative Flight Services -- the VIP Fleet. Ministers are not required to submit or retain receipts for travel expenses. Such an honour system is not susceptible to audit. However, Treasury Board advised ministers that it would be prudent to keep receipts. The Government wrote to me stating that even where receipts had been kept they would not be provided to my Office. It also stated that information on the reasons for requesting the use of the VIP fleet by ministers would also be withheld. Without this information I cannot verify that claims for travel expenses were appropriate, that government aircraft were used for official business, and that the charges, which vary by purpose, were accurate. I have therefore decided not to proceed with the audit unless I get access to the necessary information. Therefore, I am reporting here to the House of Commons that I have not received the information needed to complete the audit.

1

MATTERS OF SPECIAL IMPORTANCE AND INTEREST

1

MATTERS OF SPECIAL IMPORTANCE AND INTEREST

Main Points

1.1 The opening chapter provides the Auditor General with the opportunity to introduce his report and discuss issues he believes to be of particular importance. The chapter's overall theme is about managing public funds in a time of restraint (paragraphs 1.7 to 1.15).

1.2 It begins with a discussion of the importance of accountability, stressing that all who spend taxpayers' dollars must be answerable for how they spend them (1.16 to 1.71).

1.3 This is followed by a section on access to information for audit purposes, which focusses especially on the difficulties encountered in the audit of the 1981 acquisition of Petrofina (1.72 to 1.109).

1.4 The chapter then reports on the quality of information available to Members of Parliament. It notes problems with sovereign debts and looks at Canada's foreign exchange operations (1.110 to 1.137).

1.5 Achieving improved efficiency is the next subject discussed. The Auditor General reports on some preliminary findings from his Office's ongoing study of the efficient management of public resources; and he notes opportunities for increased efficiency identified in this year's report (1.138 to 1.167).

1.6 The chapter concludes with a short section on the importance of people, emphasizing the need for changes in the legislative and administrative framework governing the management of people in Canada's public service (1.168 to 1.184).

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MATTERS OF SPECIAL IMPORTANCE AND INTEREST

Introduction: Managing In a Time of Restraint

1.7 Managing public funds in an era of restraint. That's the theme of my opening chapter in this, my ninth annual report to the House of Commons.

1.8 The government has committed itself to a reduction in the persistent budget deficits of the last decade.

1.9 An essential dimension of deficit reduction is a tightening in the resources available to departments and other agencies of government. Throughout this report there are references to the ways in which departments are responding to these limitations.

Four Elements. And One More

1.10 In this chapter I focus on four elements that are crucial to the government in achieving the greatest value for the money it spends and important to Members of Parliament in their role of scrutinizing government expenditures; elements that take on increased significance in a period of restraint -- when each public dollar must be spent wisely and well.

1.11 The four are: the need for accountability; the importance of access to information required for audit purposes; the quality of information available to Members of Parliament; and the pursuit of efficiency itself.

1.12 To them, at the close of the chapter I add one more: the paramount importance of people.

1.13 As I write about these issues, I am aware that among my readers are many Members of Parliament who were elected for the first time to the House of Commons less than a year ago. I wish to emphasize, therefore, that this opening chapter is not intended to be an overview of the total report. It simply draws together certain themes which I believe are of particular significance to Parliament. At the same time, I hope that my words give greater coherence to the chapters that follow.

1.14 It's a long report. We have again produced a compact Main Points booklet to assist readers in locating the issues of most significance to them. And there's a videotape of the highlights.

1.15 However, I hope Members of Parliament will read the full report. Its messages are important. Many are urgent.

The Need for Accountability

1.16 In a climate of restraint, accountability really matters. Those who spend taxpayers' dollars must be more than ever aware that they are answerable for how they spend them.

In a time of restraint, those who spend taxpayers' dollars must be more than ever aware that they are answerable for how they spend them.

1.17 Answerable to Parliament itself. For Members of Parliament represent those taxpayers -- and MPs will likely be the first to hear if cutbacks in services to the public are being blamed on shortages of funds.

1.18 During my years as Auditor General I have sensed an increasing awareness throughout government of the need for good accountability practices. And in one major area, this report tells of a notable improvement in accountability.

Control and Accountability in Crown Corporations

1.19 I refer to the progress in implementing the framework for better control and accountability in Crown corporations.

The main elements are successfully in place

1.20 The 1984 amendments to the Financial Administration Act (Part X) established this greatly improved framework. This Office was consulted at the time the changes were being drafted. When they became law, I endorsed the main principles of the amendments, also pointing out that it would be important for the key players to support the principles and to work with good intent, dedication and enthusiasm to implement the new regime.

1.21 During the year, we carried out a review of the implementation and functioning of the Crown corporation control and accountability framework set out in Part X of the Financial Administration Act. Chapter 5 reports on its progress and concludes that the main elements of the framework are successfully in place. Strong and sustained attention by all concerned has contributed to this achievement.

1.22 However, there are two areas that merit further attention.

The status of exempt corporations should be clarified

1.23 The first relates to the breadth of the applicability of the framework. Eight Crown corporations are exempted for various reasons -- including their need to remain at arm's length from the government. For these eight corporations, which required budgetary funding of nearly $1.5 billion in 1987-88, control and accountability are not as consistent and rigorous as those that apply to all other Crown corporations. The arrangements for these eight corporations should be clarified and, to the extent possible in view of their specific needs, brought into line with the Part X framework.

A need for better performance measurement

1.24 Second, there is room for further progress in performance measurement and reporting. While improvement has been achieved regarding the statement of corporate objectives, more attention is needed in regard to linking subsequent performance to stated objectives. If it is important to have clearly stated objectives, it is equally important to have pertinent information on the extent to which such objectives have been met.

1.25 The enactment of this new regime was an essential step in the journey toward improved control and accountability in Crown corporations. The results of our review indicate a real advance. I am optimistic that the progress and pace of the journey can continue.

Single Audit

1.26 I now turn to an area where, in my view, if an improved audit framework were put in place, there would be better accountability for the use of public moneys.

1.27 The really big ticket items in federal government expenditures largely involve transfer payments or contribution funding to individuals, organizations, and other levels of government. Co-ordinated audit activity helps to ensure full accountability for the use of these funds.

1.28 In the case of transfer payments, mutual reliance already exists to some extent. For example, this year's audit of the Canada Assistance Plan -- reported in Chapter 15 -- describes how federal officials verify that provinces have complied with the objectives of the Plan; and how a province, when submitting its claim for the federal contribution to the shared costs, must have that claim certified by an auditor designated by the province. At the same time our audit also found some weaknesses in the verification process.

An overall approach would produce better audit coverage at less cost

1.29 An overall co-ordinated approach to auditing all federal contributions could result in strengthening audit coverage, avoiding unnecessary duplication, and significantly reducing audit costs. Co-ordination can mean using a single external auditor, or developing a framework whereby the external auditors rely on one another's work, as well as on that of the internal auditors.

1.30 The interesting thing is that as long ago as 1982 the Treasury Board announced a new policy initiative designed to eliminate duplication of audit effort and clarify the roles and responsibilities of federal officials in the audit of federal contributions. The policy advocates the use of a "single audit" approach.

1.31 The single audit is defined as a co-ordinated approach to auditing whereby auditors representing all the donors effect a single audit of the recipient. In the case of shared cost programs, the donors are usually the federal government and the provinces, and the recipients are individuals and organizations that receive federal and provincial funds pursuant to a contribution agreement. The purpose of the audit is to verify compliance with the terms and conditions of the contribution agreement and with the pertinent statutes and regulations.

1.32 The first step in making the single audit concept work is to review all federal-provincial agreements before they are signed to ensure that there are adequate audit provisions, and that the provisions contemplate, to the maximum extent practicable, the use of a single audit.

1.33 The key element is the establishing of a single audit steering group, composed of representatives from the federal and provincial departments having direct responsibility for the program. The steering group would include all the stakeholders, who would then agree on what is needed by way of audit. The group would plan, direct and monitor the single audit.

1.34 The single audit provides considerable advantages. It clarifies access, potentially improving access across jurisdictions; it clearly designates the extent of reliance of one auditor upon another auditor's work; it provides the opportunity for a better definition of the audit's scope, thus reducing the risk of gaps in the coverage; it would cause less disruption to those being audited; and it would result in significant cost savings in both person-years and dollars.

The time is now

1.35 That 1982 single audit framework -- its procedures were, in fact, published in final form in 1985 -- has been implemented only in a most tentative way. Which is a pity. Undoubtedly there are important inter-jurisdictional considerations to be worked out. Nonetheless, in these days of one taxpayer supporting three -- and sometimes four -- levels of government, it's important that all the stakeholders' audit needs are met as efficiently as possible. My own view is that the single audit should be extended, wherever appropriate, to determine if due regard was given to achieving value for money. Canadians are entitled to know that, wherever their tax dollars are being used, they are being spent prudently and productively.

1.36 In short, the time has come to test the single audit concept.

Proposed Value-for-Money Audits of Parliament

1.37 This is an issue I want to touch on -- for two reasons. First, it has generated some media attention already; so it will likely seem appropriate to readers for me to comment here. Second, because it's an opportunity for Parliament to send forth a strong message about the importance of accountability.

1.38 During the past year or so, I have had discussions with both the Senate and the House of Commons on the question of undertaking value-for-money audits. I made it very clear that my examination would in no way encroach on the legislative function of the two Houses; it would involve an audit of the administrative systems that support the legislative process.

1.39 I simply proposed that Parliament should request for its support functions the same kind of audit required in virtually all federal government entities -- no more and no less.

1.40 Although the activities of Parliament are subject annually to financial attest and compliance audits, the Senate and the Library of Parliament have never been the object of a value-for-money audit. My Office last performed a value-for-money audit of the House in 1983 as a follow-up to its first comprehensive audit in 1980.

1.41 Support for members of the Senate and the House of Commons will cost approximately $200 million this fiscal year. Yet, aside from the briefest of mentions in the Estimates and Public Accounts, there is little public description of how these funds are spent. I believe that the size of these support services, the importance of the tasks they perform and their public visibility suggest that a value-for-money audit by my Office is appropriate at this time. That the Senate and the House of Commons are unique institutions is undeniable. So I fully recognize that the manner of carrying out such audits must take into account the special nature of Parliament. Each audit report would be directed to the House concerned for action that it deems appropriate.

1.42 I am writing these words in mid-August. With Parliament recessed, discussion of the proposed audits is necessarily slowed. However, I remain confident that my ongoing consultations will result in the audits proceeding, and that they will prove useful to both Houses.

A strong message about accountability from Parliament itself

1.43 For the two Houses to agree to value-for-money audits of their support systems would represent good accountability in itself. But, in my view, it would achieve something much more important.

1.44 It would send a strong message to all other organizations and individuals using public moneys that value-for-money auditing is an important part of the accountability process.

Three Taxing Problems

1.45 There's another aspect of the need for accountability that I would like to address.

1.46 It's often remarked that the public sector does not have a "bottom line" -- that inescapable reality faced by profit-oriented companies in the private sector. Nonetheless, governments have to confront their own inexorable realities.

1.47 When a government encounters degrees of deficit and debt that threaten its very ability to govern, it must act. If it wishes to maintain approximately the same level of programs and services, it has only two options. It can increase taxes. Or it can attempt to deliver the same level of programs and services -- but more efficiently.

1.48 I will be coming later to that second option. Here I want to say something about taxes. An important consideration in establishing appropriate tax levels is to ensure that all the taxes due to the government are in fact being collected. This leads to another concern. If, under a largely self-assessing tax regime, there is any widespread perception that others are not paying their fair share, the whole tax system will eventually be threatened.

1.49 I have made reference to this issue in previous reports. Three years ago, in commenting on my Office's study of tax expenditures, I wrote that reliance on the "use of the Income Tax Act to fund programs can have a dangerous impact on the integrity of the tax system." Our 1988 audit of the tax collection function at National Revenue - Taxation revealed that there had been a serious increase in taxes deemed uncollectible.

1.50 Tax problems continue to exist. There are three serious examples in this report.

Millions more tax dollars could be collected with expanded audit coverage

1.51 Our examination, in the Department of National Revenue - Taxation, of revenue programs and source deductions (Chapter 19) reveals that increases in audit coverage since 1984-85 have resulted in substantial increases in source deductions assessed and in the amount of unreported income discovered. However, our report notes that millions of dollars in additional revenues could be collected if the Department were to further expand its coverage of payroll and non-residents.

1.52 If the government can do a more effective job of assessing and collecting taxes that are due, the need for the imposition of further taxes is reduced.

A failure to plug a tax loophole

1.53 The second tax problem involves the Department of Finance's failure to plug a loophole related to a key anti-avoidance rule in the Excise Tax Act. The full story is told in Chapter 4: Audit Notes (paragraphs 4.71 to 4.79).

1.54 The crux of the issue is that some taxpayers are avoiding tax in a way that was not intended, by entering into non-arm's length transactions solely to gain a tax advantage. The government recognizes the problem; but because it will be eliminated with the introduction of the proposed goods and services tax on 1 January 1991, has decided not to close the loophole in the interim. Instead it is offsetting the lost revenue by increased sales tax rates.

1.55 The government itself has estimated that not closing the loophole is costing the public purse between $300 million and $350 million in lost revenue each year. The increased sales tax rates mean that other taxpayers -- who are not in a position to take advantage of the loophole -- are being more heavily taxed so that the government can compensate for this lost revenue. My instinct is that because it has been known since April 1989 that no action is to be taken before January 1991 -- and that this particular door to the treasury stands wide open -- the loss in revenues may far exceed the government's own estimate.

A formidable challenge

1.56 The third taxation problem is identified in the audit of the Excise Branch of the Department of National Revenue - Customs and Excise (Chapter 18). The problem exists now. But its significance lies in its potential to escalate. I am also very aware that political sensitivities are involved; and I would caution that the words I write here should not be used out of context. The context is the full audit, as reported in the chapter.

1.57 Briefly, the audit identifies a number of weaknesses in the Excise Branch's administration of the federal sales tax. In my view, these weaknesses are of major consequence.

1.58 First, the level and scope of enforcement activities have been decreasing. One aspect of this has been a marked decline in audit coverage, in spite of the fact the Branch itself recognizes that this can threaten revenue generation. In her June 1988 Annual Management Report to the Treasury Board, the Deputy Minister wrote:

> With our reliance on voluntary compliance and deterrence through selective enforcement, we are reaching dangerous levels with respect to the risk of non-compliance.

1.59 While the Branch has recently been moving fairly vigorously in attempting to increase its audit coverage, actual progress has been slow. Another aspect of this weakness in enforcement has been a failure to ensure that all eligible taxpayers are identified and licensed. A weak licensee identification function can, of course, result in a loss of revenue. It can also result in disparity among the affected industries, with consequent damage to the integrity of the system as a whole.

1.60 Second, information on performance and compliance has not been adequate, and data have not been used to the best advantage. This has meant, for example, that the Branch has not been in a position to know the extent of non-compliance in key industries and the estimated revenue loss; or the potential effect of a declining rate of audit coverage on taxpayers' compliance.

1.61 Third, certain departmental practices have gone beyond legislation, with the potential of causing unfair treatment of taxpayers, higher compliance costs, and actual revenue loss.

1.62 Fourth, the need exists within the Branch for better tools and training. Our audit makes it clear that the Branch has not taken adequate advantage of today's technology.

We also found that some weaknesses in the training function, which this Office had previously identified in 1979, still exist 10 years later.

1.63 These weaknesses, in a Branch that generated federal sales and excise taxes of $17.2 billion in 1987-88, are serious in themselves.

1.64 But the added dimension of the problem is that the new goods and services tax is scheduled to come into effect in January 1991. This represents an unprecedented challenge. The number of taxpayers the Branch deals with will increase from 75,000 to over 1 million; and the mechanics of the new tax will be completely different.

1.65 The Branch is experiencing problems now in ensuring sufficient audit coverage, identifying potential taxpayers, and providing the necessary tools and training for its people. It is difficult to overstate the magnitude of the task it faces with the implementation of the new goods and services tax.

1.66 No one likes taxes. We all recognize their necessity. It may not be possible to construct a system of taxation that operates with perfect equality. But we have a right to a system that is as fair as possible, and that can be seen to be fair. If the perception is allowed to grow that loopholes exist for a privileged few, and that inequities and inefficiencies are enabling substantial numbers of Canadians to avoid paying their fair share of taxes, then the probity of Canada's taxation structure is put at risk.

Accountability and IMAA

1.67 In concluding this section on the need for accountability, I draw attention to the information on the progress of the Increased Ministerial Authority and Accountability (IMAA) initiative, reported in Chapter 25. The chapter itself is the follow-up to the major Financial Management and Control Study carried out by this Office in 1987.

1.68 A primary aim of IMAA is to achieve increased departmental accountability and -- at the same time and as a result -- encourage productivity improvements.

1.69 Critical to the IMAA initiative's success is putting in place adequate planning, monitoring, control, internal audit, and program evaluation systems. These, together with improved performance indicators, are needed if IMAA is to achieve its objectives.

1.70 However, our follow-up in departments concludes that meaningful cost and performance data have yet to become a working reality. Without them, IMAA's development will be limited; and an opportunity for better financial management and control within departments will also be missed.

1.71 If IMAA is indeed to result in improved accountability, there is work still to be done.

Access to Information Required for Audit Purposes

1.72 It is probably inherent in human nature to resist being held to account; and from time to time my audits are delayed by such resistance. Delays can take the form of protracted discussions about the scope of the audit or a reluctance to release certain documentation. In nearly all cases these problems are ironed out; and the audit proceeds.

1.73 But, very occasionally, audits cannot proceed because of a lack of access to needed information. This has happened once already in my time as Auditor General; and it now threatens to happen a second time. I discuss the two instances here. The first relates to the acquisition of Petrofina Canada Inc.; the second to ministerial travel.

The 1981 Acquisition of Petrofina by Petro-Canada

1.74 In 1982 and 1983, I reported on the lack of evidence that due regard for economy had been exercised in expending $1.7 billion in public funds from the Canadian Ownership Account to acquire Petrofina Canada Inc.

1.75 Beginning in 1982, many discussions to obtain information about the acquisition were held with Petro-Canada, the Department of Energy, Mines and Resources, the Department of Finance and the external auditors of Petro-Canada. I was advised that assessing of oil companies to be acquired and negotiating of acquisition price were delegated by Cabinet to Petro-Canada but that the decision to purchase was retained by ministers. I was also informed by the Chairman and Chief Executive Officer of Petro-Canada that both a pre-acquisition and a post-acquisition commercial evaluation had been conducted, but that he would not give me access to the evaluations.

1.76 In March 1984, after two years of discussions, I still had not received the information. After an extensive constitutional and legal review of the matter, I decided to invoke the access to information powers in the Auditor General Act.

The government's refusal

1.77 Since Petro-Canada had prepared commercial evaluations of the acquisition, I wrote, pursuant to section 14(2) of the Auditor General Act, to Petro-Canada on 9 March 1984 to request the evaluations and any other documents pertaining to the acquisition of Petrofina Canada Inc. that were presented to officials of the Government of Canada. On 10 April, I received a negative reply from Petro-Canada. On 16 April, I wrote to the Cabinet pursuant to section 14 (3) to advise it of Petro-Canada's failure to provide the required information, asking that Petro-Canada be directed to deliver the required information to me. By 25 May 1984, I had not received any acknowledgement of my 16 April 1984 letter. In the absence of any reply, I decided to invoke the full powers of the Auditor General Act. Pursuant to section 13(1), I wrote to the Minister of Finance and the Minister of Energy, Mines and Resources to obtain the required information. These ministers were responsible for approving the capital budget of Petro-Canada and are named in the Appropriation Acts as responsible for authorizing the expenditure of up to $1.7 billion to purchase Petrofina Canada Inc. I also wrote to the deputy ministers of these Departments, themselves members of the Board of Directors of Petro-Canada that approved Petro-Canada's recommendation to the ministers to purchase Petrofina Canada Inc.

1.78 When I did not receive the required information, I wrote on 25 June 1984 to the Prime Minister, the Right Honourable Pierre Elliot Trudeau, to bring to his immediate attention the failure of the Minister of Finance, the Minister of Energy, Mines and Resources, their deputy ministers, and Petro-Canada to provide the required information.

1.79 On 26 June 1984, I received Cabinet's decision by Order in Council declining to direct Petro-Canada to provide the required information.

1.80 On 29 June 1984, the Prime Minister replied indicating that he was in agreement with the actions of his ministers and their deputies.

Proceeding through the courts

1.81 Because no further progress was possible in respect of Petrofina Canada Inc., I reached the conclusion that it was both necessary and desirable for the fulfilment of my responsibilities to Parliament to clarify the powers of the Auditor General Act by asking the courts for an interpretation of its provisions. On 5 July 1984, I therefore commenced an action in the Federal Court of Canada, seeking the Court's assistance in obtaining the audit information that would permit me to complete the audit and report to the House of Commons.

1.82 Following the 1984 General Election, and before arguments had been heard in the Federal Court, I wrote, on 17 October 1984, to the Prime Minister, the Right Honourable Brian Mulroney, reporting on my difficulties in obtaining information to fulfil my audit responsibilities to Parliament.

1.83 On 16 November 1984, the Prime Minister replied, expressing his view that:

> In respect of your concern as to the issue raised by the case that is now before the Federal Court, I believe it is important that the courts be asked to review these issues since they are fundamental to our Parliamentary system of government. Instructions are therefore being given to Counsel to proceed with the case.

1.84 On 6 December 1985, the Federal Court of Canada found that the Auditor General was entitled to access to information, including Cabinet documents that he considered necessary to fulfil his responsibilities under the Auditor General Act. On appeal by the government, the majority of the Federal Court of Appeal reversed the decision of the Federal Court. I was granted leave to appeal that decision in the Supreme Court of Canada. The appeal was heard on 7 October 1988.

The final verdict

1.85 On 10 August 1989, the Supreme Court ruled unanimously that the appeal should be dismissed.

1.86 In his reasons for judgment, the Chief Justice, the Right Honourable Brian Dickson, wrote in part:

> The Auditor General has no recourse to the courts in the event of the refusal by Parliament, responsible Ministers, and the Governor in Council to make available to him all of the documentation he may seek in what he regards as the discharge of his responsibilities in auditing the accounts of Canada. It is reasonable to interpret s. 7(1)(b) of the Act as the Auditor General's final remedy for claimed denials of s. 13(1) entitlements. Section 7(1)(b) provides that "The Auditor General shall report annually to the Houses of Commons ... on whether, in carrying on the work of his office, he received all the information ... required." The linkage between s. 13(1) (the asserted right) and s. 7(1)(b) (the statutory remedy), and the extent to which the reporting remedy is part of a comprehensive remedial code, indicate that the remedy was meant to be exclusive. The Auditor General can report on difficulties in obtaining information at any stage, even if other remedies are simultaneously being pursued, and the House of Commons can act at any time. However, once the ss. 13 and 14 remedies have been exhausted in relation to particular information, the only remedy left to the Auditor General is the s. 7(1)(b) reporting remedy.

1.87 The decision, of course, is the final word on how the access provisions in the Auditor General Act are to be interpreted. It also gives me clear direction for the future; a point I return to very shortly. However, the Court's decision also prompts me to touch on two immediate issues -- the one general; the other specific.

A good, working relationship

1.88 The general issue is, I believe, important to restate: that the Petrofina case is exceptional; and that access is not an ongoing problem for me or my Office.

1.89 On 27 December 1985 the government, by Order in Council, directed that the Auditor General be given access to a wide range of Cabinet documents. These include all the information I normally need to fulfil my audit responsibilities. The Order in Council has resulted in a constructive relationship between the government and my Office over the past four years.

1.90 This good working relationship has, I believe, served Parliament, the people of Canada, and the government itself well. I am confident that it can continue.

Whether to proceed with the audit of the acquisition of Petrofina

1.91 The immediate, specific issue is the status of my audit of the acquisition of Petrofina Canada Inc.

1.92 I am giving the matter very careful consideration. On the one hand, there is still a lack of evidence that due regard for economy was exercised in spending $1.7 billion in public funds, one of the largest federal government expenditures in Canadian history.

1.93 However, the transaction took place eight years ago. It can be argued that to pursue the matter further would result in an audit report that will almost certainly be inconclusive, and -- at this date -- become only a footnote to what is already history. I am not at all sure that to proceed with the audit is a responsible use of taxpayers' dollars.

1.94 In addition, I have already reported fully on one of the more troubling aspects of the acquisition: the complex series of interrelated transactions that resulted in Petrofina's non-resident parent being exempted from Canadian income taxes; and which may have enabled Petro-Canada to reap substantial tax benefits. (See 1985 Report of the Auditor General of Canada, paragraphs 3.74 to 3.101.

1.95 However, readers will appreciate that I am writing these words only two weeks after the Supreme Court's decision. I am still receiving advice. The auditing we have already performed has resulted in some useful insights that could be helpful to a government -- and parliamentarians -- contemplating similar transactions in the future. There may be value in drawing together the material we have, and producing a report.

1.96 I am presently considering these options. I intend to reserve any decision until after this report is tabled. Perhaps there will then be indications from Parliament about the route I should follow.

The path forward

1.97 I return to the clear direction the Supreme Court has given me. If, in carrying out the work of my Office, I fail to receive all the information I require, the extent of my remedy is to report that fact to the House of Commons, in accordance with Section 7(1)(b) of the Auditor General Act. This I shall do.

1.98 The Chief Justice has reaffirmed, in the clearest of terms, the importance of the Auditor General's duty to report:

> The adequacy of the s. 7(1)(b) remedy must not be under-estimated. A report by the Auditor General to the House of Commons that the government of the day has refused to provide information brings the matter to public attention. It is open to the Opposition in Parliament to make the issue part of the public debate. The Auditor General's complaint that the government has not been willing to provide all the information requested may, as a result, affect the public's assessment of the government's performance. Thus, the s. 7(1)(b) remedy has an important role to play in strengthening Parliament's control over the executive with respect to financial matters.

Urgency can be a factor

1.99 One of the worldwide issues the auditing profession is presently grappling with is the problem of providing timely information. Events move so rapidly and financial decisions must be made so immediately that audit reports are often outdated by the time they appear. This is equally true of legislative auditing. Parliament needs timely information if it is to fulfil its responsibilities. The problem of reports being outdated is compounded if audits are further delayed by a lack of access to information.

1.100 In the light of the Supreme Court's decision, if denial of access should threaten one of our audits, I will seriously consider bringing the matter to the attention of the House of Commons immediately.

A Lack of Access to Information on Ministers' Travel

1.101 In 1989-90 we planned to conduct a government-wide audit of expenses claimed for travel on official government business by ministers, and accompanying exempt staff and public servants. Our audit was to include examinations of the adequacy of financial control and reporting systems for ministerial office travel; the adequacy of controls over the use of Administrative Flight Services -- often referred to as the VIP Fleet -- by ministers and staff; cost recovery by the Department of National Defence; the reliability and completeness of information on operating and overhead costs of the Fleet; and the completeness of the information available in the Public Accounts of Canada on the costs of ministerial travel.

1.102 My authority to audit ministers' travel expenses is clear. Section 5 of the Auditor General Act states that "the Auditor General is the auditor of the accounts of Canada including those related to the Consolidated Revenue Fund". These, of course, include accounts of all government departments. Travel expenses of ministers are paid out of departmental budgets.

1.103 To fulfil my audit responsibilities, my Office in April 1989 requested access to receipts and other documentation supporting ministers' travel expense claims. We also sought copies of the written requests from ministers to the Minister of National Defence for use of the VIP Fleet.

1.104 On 13 June 1989 the Privy Council Office on behalf of the Government informed my Office that the information we required would not be made available to the Auditor General.

1.105 Full details of the reasons why the information was needed to conduct and complete the audit, together with the Government's reasons for refusing access to the information, are set out in Chapter 6 of this report. The Government provided its response prior to the Supreme Court decision on 10 August 1989.

1.106 Having given the whole matter extensive consideration, I have decided -- in conformance with the Auditor General Act -- to report to Parliament that, in carrying out the work of my Office, I have not received all the information and explanations I require in order to fulfil my audit responsibilities.

1.107 I have also decided not to proceed with the audit unless I get access to the necessary information.

1.108 The message that this denial of access sends is that in matters of accountability for the use of public funds, some hold themselves out as being less accountable than others. Ministers seem to have decided that their honour system of using public funds is sufficient to satisfy the requirements of good accountability to Parliament. I think otherwise.

1.109 In a time of restraint, the message they are sending is very unfortunate indeed.

The Quality of Information Available to Members of Parliament

1.110 Without good information, Parliament cannot legislate. Without good information, governments cannot govern. Without good information, Members of Parliament cannot hold governments to account. These things have always been true. But in our technological age where good and -- equally important -- timely information is the lifeblood of large organizations, they have an increased immediacy.

1.111 The legislative auditor's world is also a world of information. As Auditor General, I must seek to verify the information Parliament receives from other sources. Where information is lacking, and it is appropriate for me to provide it, I do so.

1.112 Two chapters of this report speak in different ways about the information Members of Parliament receive: Chapter 2, audit observations on Canada's financial statements, and Chapter 13, which looks at the management of foreign exchange operations in the Department of Finance.

The Financial Statements

1.113 Among the most important pieces of information Members of Parliament receive -- especially at a time of deficit reduction and restraint -- is that contained in the financial statements of the Government of Canada. And it has been one of my continuing concerns as Auditor General to encourage the government to prepare financial statements that provide the clearest and most complete picture possible of the government's overall financial position and operating results.

1.114 We have come a long way. The federal government's statements are among the best in the world -- they may well be the best. Nonetheless, two things remain to be done.

A need for an understandable annual financial report

1.115 One step is for the government to produce annually a comprehensive but concise financial report, similar to annual reports published by large corporations in the private sector.

1.116 Our 1986 Federal Government Reporting Study showed that this kind of financial report would be of great value to many users of government financial information, notably Members of Parliament themselves. Following public hearings on the study in 1986 and 1987, the Public Accounts Committee endorsed the need for such a report. Some progress is evident in Section 1 of Volume 1 of the Public Accounts. That's good. More progress is needed and possible.

Action required to eliminate audit reservations

1.117 The second course of action I urge upon the government is to make the accounting policy changes that would allow me to remove the three reservations from my audit opinion on the government's overall financial statements.

1.118 One of the three reservations is concerned with the risk inherent in the government's sovereign loans; the second relates to the government's failure to include Crown corporations within the reporting entity; the third involves unrecorded employee pension liabilities. Background information on the three reservations can be found in paragraphs 2.40 to 2.65 of this report.

1.119 These reservations have been around a long time. I had hoped they would be eliminated by now; but the government continues to study the matter. I encourage the Minister of Finance in his 1990 Budget to announce revisions to the government's accounting policies. That would give me the opportunity of removing the reservations before I step down as Auditor General on 31 March 1991.

A particular concern with the problem of sovereign loans

1.120 Intense interest is presently focussed world-wide on the consequences of sovereign debt, in which Canada is an important player. So I want to summarize here my concerns as Canada's auditor.

1.121 The Government of Canada has many dealings involving financial transactions with governments of other nations. The Canadian Wheat Board sells grain; the Export Development Corporation lends money; and through the Canadian International Development Agency, the government makes concessional loans.

1.122 It is not unusual for other national governments to owe money to the Canadian government. For the most part, these sovereign loans have been paid on time and in full.

1.123 However, as with sovereign loans owed to commercial banks, some have not been paid on time and some may not be paid in full. Financial loss seems likely. Neither the government nor the banks are immune. And, although the government directs commercial banks to include the risk of loss on sovereign loans in their financial reports, it does not do so itself.

1.124 As a result, I believe that certain of the government's financial reports are misleading. They include the overall financial statements of the government and the financial statements of the Export Development Corporation. Paragraphs 2.41 to 2.56 and 4.17 to 4.19 of this report provide detailed comments on these statements.

1.125 The government seems to believe that it does not face any risk of loss on sovereign loans -- that any repayment arrears can be eliminated by rescheduling the amounts due.

1.126 Under rescheduling, if a debtor falls behind on interest, the government may convert the interest to principal. If a debtor falls behind on principal, the government may adjust repayment dates or provide a repayment "holiday". Rescheduling is not a problem in itself; it is an accepted international mechanism that governments use in trying to work out repayment difficulties.

1.127 The problem is that rescheduling is used as a shield to hide from public scrutiny losses the government has suffered or is likely to suffer on its sovereign loans. Paperwork disguises reality.

1.128 The government's policy is to recognize a loss on sovereign loans only if a nation formally repudiates what it owes or the debt is forgiven. In my view, this is far too late. If a sovereign loan falls into arrears and is rescheduled time and again, the reality is that there is a substantial risk that amounts owing to the government will ultimately not be repaid.

1.129 This risk of loss should be included in the government's financial reports as soon as it is recognizable. There is no simple right answer for the amount of losses that should be booked. But prudence requires that some reasonable amount be included in published financial reports to keep them from being misleading.

1.130 A recent study submitted to the Public Accounts Committee of the United Kingdom recommended that the risk of loss on sovereign loans be included in the government's published financial report. The study concluded that there was no clear difference between the government and commercial banks. Although objectives differed, prospects for recoverability did not. Accordingly, the study recommended that the risk of loss on sovereign loans be determined according to commercial banking practice. The United Kingdom Public Accounts Committee endorsed the recommendations, and the risk associated with sovereign loans was acknowledged in the accounts.

1.131 The International Monetary Fund and the World Bank -- two of the largest sovereign lenders in the world -- now recognize the risk of loss on sovereign loans in their published financial reports. In my view, our government should follow the same course and revise its accounting for sovereign loans at the earliest possible date.

Shedding Light on Foreign Exchange Operations

1.132 In my close to nine years as Auditor General, I have been made aware that some of the best intelligence Members of Parliament receive on certain government activities comes from the pages of this Office's annual reports, which, in providing audit information, also give a succinct picture of the program we have examined.

1.133 This year's study of the Department of Finance's foreign exchange operations (Chapter 13) is a good illustration. It depicts, conveniently and clearly, Canada's intervention activity relative to foreign exchange.

1.134 The audit may also raise some interesting questions for Members of Parliament: Are Canada's foreign exchange reserves too high, too low, or just right? What are the overall net costs of holding such reserves? What are the assumed benefits? What are the real benefits? Are reserves really necessary for intervention? Is intervention itself necessary? Are the high costs of holding gold reserves justified? Is the rationale for restricting the currencies in which reserves and foreign debt are held correct and appropriate? What is its cost?

1.135 But, in considering these issues, more comprehensive questions must surely also surface: How much does Parliament really know about foreign exchange management? What opportunity is provided for Members of Parliament to examine and debate these operations?

1.136 Our audit reveals the inadequacy of the information that Parliament receives about this important macroeconomic policy area.

1.137 Only with such comprehensive, consolidated information on these matters, can Members of Parliament fulfil their task of scrutinizing the activities of government.

The Pursuit of Efficiency

1.138 I wrote earlier that there are two options available to a government that wants to tackle the deficit and debt without curtailing programs. It can increase taxes. Or it can operate more efficiently.

1.139 It is the latter course that taxpayers surely favour: to see their government promoting greater efficiency and productivity throughout departmental programs; achieving the same -- or an enhanced -- measure of services, using fewer resources.

1.140 A key element in my audit mandate is to identify cases where insufficient regard has been given to achieving efficiency. Wherever appropriate, I report such instances in a constructive way; identifying opportunities for improved efficiency.

An Ongoing Study of Efficient Management of Public Resources

1.141 Several chapters in this report note such opportunities. This is not entirely fortuitous. A year ago I initiated a major study on the efficient management of public resources. Its results will appear in next year's report. Meanwhile, specific opportunities for increased efficiency are already surfacing. I will come to them in a moment.

1.142 One of the areas our study will be examining is the overall stance of the government toward achieving more efficient management. Senior managers in both the central agencies and departments have an important role to play in creating an environment that is conducive to efficient management. It is crucial that this environment foster both the level and quality of leadership required, as well as encouraging the development of an infrastructure and management practices that actively and successfully pursue efficiency improvement opportunities.

1.143 I also emphasize that efficient management and use of public resources are the ongoing responsibility of managers in the public service, restraint or no restraint.

Central agencies and departments have parts to play

1.144 In initiating our study we were aware of the history of changing government management philosophies over the years. The 1962 Royal Commission on Government Organization (Glassco) pushed for decentralization: "let the managers manage". The 1979 Royal Commission on Financial Management and Accountability (Lambert) emphasized the need for centralized control, largely because the existing management environment did not provide sufficiently for accountability.

1.145 The initiative of recent years, Increased Ministerial Authority and Accountability (IMAA), is intended to provide greater departmental authority; with something of a "hands-off" approach by central agencies.

1.146 IMAA's objective of giving departmental managers more responsibility and the means to exercise that responsibility -- while at the same time reducing the time-consuming demands of process and procedure -- accords with the findings of three of my Office's previously reported studies: "Constraints to Productive Management in the Public Service" (1983); "Financial Management and Control Study" (1987); and "Attributes of Well-performing Organizations" (1988). And IMAA has already achieved results, especially in decreasing the burden of administrative controls.

1.147 However, our Financial Management and Control Study (FMCS) also contained cautions about IMAA; specifically, that its successful implementation was "going to be relying on certain existing mechanisms -- mechanisms that we have found don't work well" And our FMCS follow-up audit (Chapter 25) suggests that IMAA's progress is, in important respects, at something of a critical point in gaining the momentum that can result in improved accountability.

1.148 What is emerging from our present study on efficiency improvement is the need for a balanced management framework; one that provides central agencies and departments with complementary, yet separate and distinct roles and responsibilities. There appears to be a need for a co-ordinated, team approach to handling the complexities of maintaining services while employing reduced resources.

1.149 The management framework for efficiency improvement involves a series of steps.

1.150 The pursuit of efficiency must begin with a shared vision of what is practical and achievable. Clearly, both central agencies and departments have roles in generating this commitment, and providing the needed guidance and support. And we will be asking such questions as whether senior management in both the central agencies and departments really see the pursuit of efficiency as something they are expected to achieve, and for which they will be held accountable.

1.151 While it is primarily the responsibility of departments to identify and analyze opportunities for improved efficiency, the central agencies also have a role in the next step of identifying government-wide initiatives and co-ordinating the learning experience of individual departments. I am particularly interested in knowing if, in the face of restraint, departments are encouraged to identify other areas where economies can be made, before deciding to cut levels of service.

1.152 Our study will then move in to examine the final three steps that begin with the implementation of actual efficiency improvements; the establishing by the central agencies of information requirements and the vital putting in place of adequate reporting systems by departments; and, finally, the shared responsibility of evaluating individual departmental and overall government progress in achieving greater efficiency and productivity.

Opportunities for Increased Efficiency

1.153 I want our study -- and our future auditing -- to identify opportunities for increased efficiency; to identify ways of increasing output despite constraints in resources.

The government is not taking full advantage of today's technology

1.154 These opportunities do exist. Our audit of the management and use of telecommunications (Chapter 7) concludes that significant potential savings in costs are not being achieved. At a time when telecommunications have a vital role in ensuring the efficient delivery of services, the government is providing no clear leadership to departments. This may mean that the government will be unable to take full advantage of the technological innovations coming on stream in this all-important area. The danger, of course, is -- with deficit financing -- that the government can be spending tomorrow's money today: only to find that it is addressing yesterday's problems.

Potential savings in marine operations

1.155 But opportunities for increased efficiency are by no means confined to high-technology areas. Our audit of Fleet Management (in Chapter 23: Department of Transport - Canadian Coast Guard) reveals that there is the potential for major savings in the $183 million operating costs and the $2.5 billion replacement costs of the 46-vessel fleets.

1.156 For most of its vessels the Coast Guard uses a crewing system based on normal office hours -- eight-hour day; five-day week -- rather than one that matches the opportunity to use these ships as efficiently as possible. Normally, Coast Guard ships return to their home ports and tie up for weekends and public holidays. When icebreakers and other vessels are berthed for extended periods for maintenance or modernization, they continue to be fully crewed. For example, one ship remained fully crewed for a 37-week period of inactivity in 1987-88 at an average weekly cost of $25,775.

1.157 There is an urgent need for the Coast Guard to strengthen its analytical capability. Our analysis of the workload and the capacity of the aids to navigation fleet for the 1987-88 peak period revealed that the work could have been done by at least five fewer ships with no discernible reduction in the service currently being provided. The annual operating costs of these five ships was $10.9 million while their replacement costs amount to some $169.1 million dollars.

1.158 What is also puzzling, as noted in our report on the Canadian Coast Guard (Chapter 22), is that the Coast Guard has allocated few resources to performing essential inspections of safe operating practices of commercial fishing vessels, foreign ships carrying dangerous goods, or passenger ferry operations.

Poor quality assurance practices have major consequences

1.159 Poor quality assurance practices can have a significant and long-term impact on efficiency. The objective of our audit of Quality Assurance (Chapter 16) was to determine whether the quality assurance systems and practices in selected contracts conformed with generally recognized national and international standards for quality assurance.

1.160 The Government of Canada spends more than five billion dollars annually on a variety of goods. To ensure the quality of these products it has traditionally relied on product standards, inspection and warranty. These methods have been adequate for low technology and high volume production, but appear to be inadequate when dealing with higher technology and complex products that require a more comprehensive approach to quality assurance. That is not a happy situation in itself; inferior product quality can affect the efficiency of government services.

1.161 But there is a more sweeping repercussion. If, as the single largest purchaser of Canadian goods, the government accepts inferior products, it is in effect endorsing a failure to achieve quality by our industries. The federal government is not their only customer. Those industries must also compete in an increasingly difficult international market demanding high standards. The government has a responsibility to encourage a more rigorous approach to quality. The result will be to enhance the reputation and competitiveness of Canadian industry, both at home and in the international market.

Restraint should generate greater efficiency; before cutting levels of service

1.162 One of the questions surfaced by our current efficiency study is: in the face of restraint, do some departments look to cutting levels of service before trying to identify more efficient ways of achieving the required levels?

The challenge is to provide more efficiently the government programs Canadians deserve, need, and have paid for.

1.163 In the private sector the demands of a bottom line mean that -- when bad economic times strike -- fat is cut from the company's administrative centre. The one sacrosanct area is where the company's products meet its customers.

1.164 In the government sector the reaction to restraint is too often the exact opposite. The immediate cry is that services to the public must be curtailed.

1.165 This year's audit of the Canadian Parks Service (Chapter 11) illustrates my point. Although not well measured, there is a perceived decline in the quality and extent of services being provided to visitors to our national parks. The Parks Service attributes this decline to an overall reduction in its person-year resources.

1.166 But our audit goes on to identify a number of opportunities to increase efficiency by reducing person-years in overhead and support functions -- such as finance and administration -- which could be reallocated to service areas.

1.167 A changed mindset is needed throughout government. In a time of restraint, the needs of the government's client community -- the taxpayers of Canada who ultimately pay all the government's bills -- must come first.

People. The Most Important Resource of All

1.168 The underlying theme of this opening chapter has been that of managing in a time of restraint. My focus has been on the need for better accountability, the importance of access, improved information for Members of Parliament, and recognizing opportunities for increased efficiency. But I am well aware that these things in themselves are not enough.

1.169 There's a need for leadership. There's a need for a shared vision by all who are delivering government programs and services. There's a need for the kind of actions that demonstrate a conviction that people are indeed important. Competent and motivated public servants can identify and act on opportunities for achieving greater efficiency.

A Changing Environment

1.170 The public service faces external and internal challenges. Globalization of the economy, free trade, environmental issues, the arrival of the information era, changes in societal values, and an increased demand for a greater variety of services are some of the significant external factors. Coping with such changes requires the ability to adapt quickly, which in turn requires a more flexible approach to the management of the people in the public service.

1.171 Among the internal challenges is the fact that, with restraint in place, there has been limited recent recruitment at entry level. This has been reported by the Public Service Commission. It is imperative that the public service attract, motivate, and retain the bright minds -- at ease with today's technologies -- who can adapt to and take advantage of the emerging opportunities for improved efficiency.

A Need for Reform

1.172 Chapter 8 provides a follow up to our 1987 audit of the Management Category. Chapter 9 reports on the government's Incentive Awards Plan. These chapters, together with our 1983 study on constraints to productive management, our ongoing study of efficiency, our 1988 study of the attributes of well-performing organizations, and many other references in this year's and previous years' chapters, all point to one inescapable conclusion.

1.173 For the federal public service to be able to meet the challenges that the future holds, there is a need for reform of the legislative and administrative structure that governs people. There is a need to bring a creative new outlook to the management of Canada's public servants.

1.174 A number of countries, including the United Kingdom, Australia, the United States, and New Zealand, have faced up to a similar situation in recent years; and each has made significant, even radical, changes in the roles and responsibilities of those who manage their public service.

1.175 But on the federal scene in Canada the basic legislative and administrative framework governing the management of people has basically remained unchanged for more than 20 years. And what has further complicated the situation has been the constant addition of layer upon layer of separate pieces of legislation -- dealing with such undeniably important things as official languages, employment equity, and access to information -- which have made the coherent management of the people in the public service extremely difficult.

1.176 Our auditing over the years indicates that there is a prevailing view that the correct application of administrative systems and practices will result in effective management and the best use of people. Our work does not support this view. Our overall observation is that people are over-administered -- too much centralization; too many prescriptions -- while, all too often, they experience a lack of real leadership. Systems and practices only work well when they are aligned with and supported by strong leadership, shared values, and an enlightened management philosophy that is consistently communicated and reinforced through day-to-day decisions and actions.

Governments have been only playing at the margins: new legislation is required

1.177 There is an awareness among many senior officials of the need for wide-ranging changes; and some progress is being made. But the impact of these changes is seriously diminished because of the overly complex legislative and administrative framework now in place. Furthermore, some specific changes -- for example, a clearer identification of the management cadre -- cannot be made without altering legislation. What is required is a simplifying of the institutional framework; and a streamlining of the ways human resources are managed. Successive governments have been only playing at the margins of the problems. Despite announcements that legislative changes were imminent, nothing has happened. For example, in 1983 we decided not to proceed with an audit of the management of staffing because we were told that important changes to the Public Service Employment Act would come into effect before the completion of the audit. We are still waiting for those changes -- six years later! If the government is serious about achieving more productive management, the time has come to act.

1.178 That action -- I respectfully suggest to Members of Parliament -- should begin with new legislation. Many aspects of the legislation presently governing human resource management have been the subject of criticism or legal challenge. There is a need for unified, overall legislative reform.

1.179 It's not my place to attempt to spell out the particulars of that reform. However, key elements in the legislative changes made in other jurisdictions include simplification of the structure at the centre to provide for a focal point and leadership; with delegation to departments of authority, autonomy, and responsibility, for the management of their human resources. In developing new legislation for the Canadian public service, these same issues should be considered.

1.180 Creating an environment in which people at all levels are involved, committed, and feel a sense of their own worth is crucially important in adapting to changing times. It is people who cope with change and who use change to achieve new levels of excellence.

1.181 Next year, in my final report as Auditor General, I will be publishing the conclusions of our study on the efficient management of public resources. The report will also contain the results of another study, titled "Management Values", which will discuss the impact of values on performance in the public service.

1.182 The two go together. If the government can initiate the changes needed to bring a new direction to the way it manages its people; if it can achieve a greater flexibility throughout the public service; if it can establish shared values and shared objectives; if it can provide clear leadership and a sense of vision; then it can maintain the Canadian federal public service as among the best in the world.

1.183 At the same time, the government can achieve those efficiencies which, despite restraint, will enable it to provide Canadians with the quality of services and programs they deserve and need.

1.184 And which -- through their taxpayers' dollars -- they have paid for.

2

OBSERVATIONS BY THE AUDITOR GENERAL ON THE GOVERNMENT'S FINANCIAL STATEMENTS AND PUBLIC ACCOUNTS

2

OBSERVATIONS BY THE AUDITOR GENERAL ON THE GOVERNMENT'S FINANCIAL STATEMENTS AND PUBLIC ACCOUNTS

Main Points

2.1 The financial statements of the Government of Canada are included in Section 2 of Volume I of the Public Accounts. These financial statements continue to be based on certain accounting policies that I believe are inappropriate. As a result, the statements:

- do not include sufficient allowance for Crown corporation borrowing (paragraphs 2.41 to 2.56);
- do not include Crown corporations in the reporting entity (2.57 to 2.61); and
- do not include the full liability for indexing of employee pensions (2.62 to 2.65).

2.2 These are not just technical matters, of interest only to accountants. In my opinion, the result of using these inappropriate accounting policies is that the government's financial statements do not reliably inform parliamentarians and others who read them (2.24 to 2.39).

2.3 In November 1988, the Canadian Institute of Chartered Accountants' Public Sector Accounting and Auditing Committee issued two new pronouncements. Measures recommended in these pronouncements, if implemented by the government, would resolve my concerns with the government reporting entity and with the liability for indexing of employee pensions (2.15 to 2.23).

2.4 Important features of the Canadian system of governing -- consent of the governed, an executive entrusted with great powers, imposed limits on executive powers, and oversight of executive actions -- depend in part on the availability of good financial information. The Public Accounts of Canada are a major source of annually reported financial information (2.66 to 2.72).

2.5 However, the Public Accounts do not include a comprehensive but concise annual financial report similar to annual reports published by corporations in the private sector (2.73 to 2.81).

2.6 In addition, the Public Accounts use inconsistent accounting and classification practices, which make it difficult to compare actual with forecast results or to move easily between summary-level and detailed information (2.82 to 2.93).

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My audit opinion on the government's financial statements continues to include three significant reservations. In my view, the government's statements do not present information fairly. In addition, the Public Accounts, which contain the statements, are complex and difficult to use. (2.7)

The Canadian Institute of Chartered Accountants' Public Sector Accounting and Auditing Committee 2.15

Implementation of accounting recommendations issued by the Canadian Institute of Chartered Accountants' Public Sector Accounting and Auditing Committee would help the government present information fairly. (2.15)

Background Information on My Audit Opinion 2.24

In giving my opinion on the government's financial statements, it is important to realize that I am not guaranteeing the absolute accuracy of the statements. Every year, the government enters into millions of transactions involving many billions of dollars. Errors do creep in, and some may go uncorrected. When I audit the government's statements, I seek reasonable assurance that they do not contain errors whose total effect would be material enough to mislead the reader. (2.24)

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Important features of the Canadian system of governing depend in part on the availability of good financial information. The Public Accounts are a major source of annually reported financial information (2.66)

The Need for a Concise Annual Financial Report 2.73

Publication of a comprehensive but concise annual financial report, similar to annual reports published by corporations in the private sector, would help parliamentarians and others obtain a complete picture of government without getting buried in massive amounts of detail. (2.73)

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More consistency in accounting and classification practices within the Public Accounts would make it easier to compare actual with forecast results and to move between summary-level and detailed information. (2.82)

Exhibits

2.1 An Illustration of Inconsistent Accounting and Classification

2.2 Illustration of the Difficulty of Linking Detailed and Summary Information in the Public Accounts

OBSERVATIONS BY THE AUDITOR GENERAL ON THE GOVERNMENT'S FINANCIAL STATEMENTS AND PUBLIC ACCOUNTS

Introduction

My audit opinion on the government's financial statements continues to include three significant reservations. In my view, the government's statements do not present information fairly. In addition, the Public Accounts, which contain the statements, are complex and difficult to use.

2.7 The financial statements of the government for the year ended 31 March 1989, and my audit opinion on them, are in Section 2 of Volume I of the Public Accounts of Canada. In this chapter, I present additional information and comments on the government's financial statements and my audit opinion. I also comment on the role of the Public Accounts and offer two suggestions for their improvement.

2.8 The government's financial statements convey a highly summarized financial overview of its various activities. The overview includes the government's cash balances and investments together with amounts owing to and by the government at the end of the year (its financial position); its revenues and expenditures for the year (the results of operations); and the extent to which cash going out exceeded cash coming in (the government's financial requirements).

2.9 My audit opinion tells readers about two matters. First, whether the financial statements were prepared according to the government's accounting policies, applied consistently from year to year. Second, whether users of the statements can rely on them to present fairly the government's financial position, results of operations and financial requirements.

2.10 As in 1988, I have concluded and reported that the government's financial statements do not present fairly its financial position, results of operations and financial requirements. The reason is that three of the accounting policies used by the government in preparing the statements are, in my judgment, inappropriate.

2.11 During the fiscal year, the Canadian Institute of Chartered Accountants' Public Sector Accounting and Auditing Committee (PSAAC) issued two new pronouncements. Measures recommended in these pronouncements, if implemented by the government, would resolve my concerns about two of the three accounting policies that I believe are inappropriate.

2.12 Important features of the Canadian system of governing -- consent of the governed, an executive entrusted with great powers, imposed limits on executive powers, and oversight of executive actions -- depend in part on the availability of good financial information. The Public Accounts of Canada are a major source of annually reported financial information.

2.13 In 1986, published results of a research project undertaken jointly by my Office and the United States General Accounting Office indicated that parliamentarians and others need a comprehensive but concise annual financial report, similar to annual reports published by corporations in the private sector. The government has not developed such a document, although some progress has been made in reshaping Volume I of the Public Accounts of Canada.

2.14 The Public Accounts are complex and difficult to use. Inconsistencies in accounting and classification practices make it difficult to compare actual results with forecast results or to move easily between summary-level information and detailed program accounting information. The complexity can be reduced by making appropriate changes to accounting practices used to prepare departmental Estimates.

The Canadian Institute of Chartered Accountants' Public Sector Accounting and Auditing Committee

Implementation of accounting recommendations issued by the Canadian Institute of Chartered Accountants' Public Sector Accounting and Auditing Committee would help the government present information fairly.

2.15 At present, the federal and provincial governments in Canada prepare their financial statements in accordance with accounting policies that each has developed. These policies differ from government to government. As a consequence, it is difficult for those who use the financial statements to compare one government with another.

2.16 It is also difficult for those who prepare and audit government financial statements to know when they are presenting information fairly and when they are not. Although a framework is now in place, there is not yet an agreed-upon set of standards for good accounting and reporting practice, to help users get the information they need and to help preparers and auditors assess fairness.

2.17 In March 1981, the Board of Governors of the Canadian Institute of Chartered Accountants established the Public Sector Accounting and Auditing Committee (PSAAC). The 19-person committee is composed of senior public sector officials, public accountants and academics. Public sector officials include deputy ministers, comptrollers and auditors general and senior executives of government-owned corporations from federal, provincial and local governments. Input and advice is sought from about 100 other people, including users, preparers and auditors of government financial statements. PSAAC provides a forum for considering the needs of users, preparers and auditors, and an opportunity to develop and recommend enhanced accounting principles and disclosure standards for consideration by Canadian governments and their legislative auditors.

2.18 The existence of PSAAC does not alter the responsibility of legislative auditors to exercise independent professional judgment when they examine and report on government financial statements. However, PSAAC can help legislative auditors discharge this responsibility better by developing a consensus view of appropriate financial reporting practice that both governments and auditors can refer to in assessing fairness. The result should be financial statements and audit reports that are more attuned to user needs and more comparable, both over time and from government to government.

2.19 During the fiscal year, PSAAC completed a framework for generally accepted accounting principles and financial reporting standards appropriate for governments. This framework comprises the following three pronouncements on accounting:

Accounting Statement 2 (1984)	identifies five objectives of government financial statements;
Accounting Statement 3 (1986)	sets out 35 general reporting principles and disclosure standards for information in government financial statements; and

Accounting Statement 4 (1988) addresses the principles and criteria for determining which activities should be included in government financial statements, and how these activities should be accounted for if they are brought in.

2.20 PSAAC also issued Accounting Statement 5 in November 1988 dealing with accounting for employee pensions. In addition, a research study on the recording and reporting of physical assets has now been completed. Another project, examining how governments should account for and report transfer payment programs, is well under way.

2.21 The financial statements of the government comply with all but four of the principles and standards recommended in Statement 3. Those recommended in Statements 4 and 5 have not yet been implemented. They are the subject of Reservations 2 and 3 in my audit opinion on the government's 1989 statements.

2.22 The recommendations in PSAAC Accounting Statement 3, with which the government's financial statements do not yet comply, require:

- a statement of changes in financial position;
- disclosure of the government's acquired physical assets on hand and available for use at the end of the year;
- a comparison of actual results with those originally forecast by the fiscal plan; and
- revenues to be accounted for on the accrual basis where practicable.

I have not yet added a reservation to my audit opinion on the government's statements because of its failure to implement these recommendations. However, I believe that they are sound, and I would encourage the government to implement them at the earliest possible date.

Implementation of PSAAC's recommendations would improve the government's financial statements and should help eliminate the need for reservations in the Auditor General's opinion.

2.23 I support PSAAC and recommend its pronouncements to both the government and to parliamentarians.

Background Information on My Audit Opinion

In giving my opinion on the government's financial statements, it is important to realize that I am not guaranteeing the absolute accuracy of the statements. Every year, the government enters into millions of transactions involving many billions of dollars. Errors do creep in, and some may go uncorrected. When I audit the government's statements, I seek reasonable assurance that they do not contain errors whose total effect would be material enough to mislead the reader.

2.24 In the next four sections I consider in more detail what my audit opinion on the government's financial statements means and how I arrived at it.

Mandate for My Audit of the Government's Financial Statements

2.25 The mandate for my audit of the government's financial statements is contained in section 6 of the Auditor General Act. Section 6 states that "the Auditor General shall examine the several financial statements required by section 64 of the Financial Administration Act to be included in the Public Accounts, and any other statement that the President of the Treasury Board or the Minister of Finance may present for audit and shall express his opinion as to whether they present fairly information in accordance with stated accounting policies of the federal government and on a basis consistent with that of the preceding year together with any reservations he may have".

An Overview of My Audit Opinion

2.26 My audit opinion on the government's financial statements consists this year of two paragraphs followed by three reservations. The first paragraph, commonly referred to as the "scope" paragraph, identifies the financial statements that I have examined and reported on and the nature and extent of the audit work that I have performed. The second paragraph, commonly called the "opinion" paragraph, contains my conclusions about the government's financial statements.

2.27 The scope paragraph. The scope paragraph begins by listing the financial statements covered by my opinion. These financial statements, and the information they convey, are summarized below. The Statement of Use of Appropriations that was presented for audit in the past has been replaced by a summary note to the financial statements (Note 3) in the current year. Details respecting the use of appropriation authorities continue to be presented in Volume II (Part I) of the Public Accounts.

Financial Statement	**Information Conveyed**
Statement of Transactions	the extent to which cash going out exceeded cash coming in (financial requirements)
Statement of Revenue and Expenditure and Accumulated Deficit	what the government's revenues and expenditures for the year have been (results of operations)
Statement of Assets and Liabilities	the government's cash balances and investments, together with amounts owing to and by the government at the end of the year (financial position)

It is important to note that my audit opinion relates only to these summary financial statements and related notes contained in Section 2 of Volume I of the Public Accounts of Canada. It does not extend to the more detailed information presented in other sections of the Public Accounts Volume I, or to Volumes II and III.

2.28 The scope paragraph concludes by stating that my audit work on the government's financial statements has been conducted according to generally accepted auditing standards prescribed by the Canadian Institute of Chartered Accountants. I use these standards to ensure that my audit is conducted with appropriate rigour and professionalism.

2.29 The opinion paragraph. The opinion paragraph contains my conclusions about two matters. First, whether the financial statements were prepared in accordance with the government's stated accounting policies consistently applied. Second, whether the financial statements may be relied on to present fairly the government's financial position, results of operations and financial requirements. If I conclude that the statements inform readers reliably, I state that information is "presented fairly"; if they do not, I use the phrase "do not present fairly", and add supporting "reservations" to explain why.

2.30 This year, as in 1988, I have concluded and reported that the financial statements have been prepared in accordance with the government's stated accounting policies. But I have concluded that these stated accounting policies result in a display of information about the government's overall financial position, results of operations and financial requirements that is not reliable. The overall effect on the government's financial statements is not fully determinable. However, each of the statements is materially affected. As a result, I continue to report that the financial statements do not present information fairly, for the reasons set out in three reservations.

2.31 I have made two changes to my opinion paragraph this year. First, I have concluded and reported that the government's stated accounting policies have been consistently applied with one exception. As disclosed in Note 4 (ii), the accounting for income tax refunds has changed. Second, I have deleted reference to the Statement of Use of Appropriations because it has been replaced by a new summary note (see paragraph 2.27).

Materiality and Audit Assurance

2.32 In planning my audit of the government's financial statements, I consider two main factors that determine the nature and extent of the work required. The first of these is a dollar figure called "materiality". This represents a threshold: if total errors fall below this threshold, the financial statements present information fairly; if they exceed this threshold and are not corrected, I refer to them in reservations to my opinion. The second factor is a percentage figure called "audit assurance". This represents how certain I want to be that my audit will reveal total errors that equal or exceed the materiality threshold.

2.33 At the conclusion of the audit, I determine whether the effect of uncorrected errors in the financial statements would mislead those who use the statements. If the effect would be to mislead, I include a reservation in my audit opinion.

2.34 In conducting my audit, I cannot be 100 percent certain that it will reveal all errors in the financial statements that, individually or in total, may be material. The size and complexity of the government, as well as cost considerations, make it impractical for me to examine all or even most of the $1.5 trillion-worth of individual transactions entered into during the year.

2.35 What I can do is verify samples of transactions and account balances, determine whether significant financial controls within the government are working and can be relied on to produce complete and accurate data, and carry out other procedures -- such as confirming year-end balances with third parties and performing analyses -- to identify anomalies in the reported data.

2.36 What this comes down to is exercising professional judgment about how much auditing is required to provide reasonable assurance to users of the statements that they can rely on reported results and not be misled.

Auditing for Compliance with Parliamentary Authorities

2.37 As part of my audit of the government's financial statements, I examine and verify compliance with parliamentary authorities to spend, borrow and raise revenues. I do this to the same level of materiality and audit assurance as that established for my audit of the government's overall financial position, results of operations and financial requirements. However, this level of materiality is significantly larger than many of the authorities being audited.

2.38 For example, spending authority is granted by Parliament in Appropriation Acts, commonly called votes. There were over 400 in the current year. Many departments are responsible for several votes, whose size and complexity vary greatly. Votes range in size from a few thousand dollars to several billion dollars. It would not be practical for me to audit each vote every year to a level of materiality appropriate to its size.

2.39 I have therefore decided to perform detailed verifications of individual authorities on a cyclical rather than an annual basis. The results of this work are included in the applicable chapters in this annual report to Parliament.

Background Information on the Reservations in My 1989 Audit Opinion

2.40 The next three sections present background information on the three reservations stated in my audit opinion on the government's 1989 financial statements.

Reservation 1: Failure to Provide for Crown Corporation Borrowings

This reservation concerns the Canadian Wheat Board, an agent Crown corporation that is not included in the government's financial statements. The government has guaranteed the Board's borrowings, so it is responsible if the Board cannot pay. In my judgment, the value of the Board's recorded assets is not sufficient to repay its borrowings. I believe that an allowance for at least $1.5 billion of the Board's borrowings should be recorded in the government's statements.

2.41 The Canadian Wheat Board (CWB) buys grain from Canadian farmers and sells it on the world market. Under the CWB Act, any profit on operations is distributed to farmers, with any loss being absorbed by the government. The terms of sales generally specify cash on delivery. However, credit sales are also made, but only with the concurrence of the government and within guidelines it has established. The Board finances its accounts receivable from credit sales by borrowing. CWB's borrowings are fully guaranteed by the government. Repayment of its borrowings depends on receipt of payment for its credit sales.

2.42 As described in Note 13 to the government's financial statements, the CWB has borrowed $3.7 billion, mainly to finance these accounts receivable. On 31 March 1989, CWB was owed approximately $3.2 billion in accounts receivable from countries experiencing difficulties in repaying their debts. Included in this figure is about $1.5 billion of interest that CWB has charged the countries. More than one half of this accrued interest has been converted to new principal by CWB at the direction of the government. This was done as part of debt rescheduling to ease the financial burden on countries experiencing repayment difficulties. These difficulties continue and, in some cases, further debt rescheduling is expected.

2.43 I believe that the reported value of amounts receivable from sovereign states has been impaired, putting the government at risk for some portion of CWB's borrowings.

2.44 An allowance has not been established in CWB's financial statements for reducing the value of amounts owed by countries experiencing repayment difficulties, and interest revenue on these amounts is still being recorded in the accounts. This is being done even where payments are not being received. The reason given by the Board for not establishing a valuation allowance for these receivables is that the government is at risk, not CWB, should any of the Board's receivables prove uncollectible. (See Chapter 4 paragraphs 4.10 to 4.16 that deal with a related concern).

2.45 According to the accounting policy stated in Note 1(vii) to the government's financial statements, amounts receivable from sovereign states are not reduced in value unless a state has formally repudiated its debts. But why would a country formally repudiate its debts when a rescheduling agreement can be obtained that spreads out repayments over an extended period and includes a grace period of several years? Moreover, converting past due interest to principal does not necessarily create assets with value, as the Estey Report on the collapse of the Canadian Commercial Bank and the Northland Bank has pointed out.

2.46 The government has used the accounting policy stated in Note 1(vii) to determine whether assets of agent Crown corporations have sufficient value to repay corporate borrowings. If borrowings exceed a corporation's ability to repay, a liability is recorded by the government under the accounting policy in Note 1(i). The purpose of this policy is to recognize borrowings that the government will likely have to repay. However, application of this accounting policy does not permit the risk associated with CWB borrowings to be recognized, because the countries that owe money to the Board have not formally repudiated their debts.

2.47 I believe that the government should provide an allowance for some portion of CWB's borrowings. The allowance would recognize the risk to the government of countries with repayment difficulties not repaying CWB. There are many methods that may be considered in determining the risk of loss on sovereign debts. Most have been developed to value sovereign debts owed to commercial banks. This does not necessarily make them inappropriate for governments.

2.48 A study recently submitted to the Public Accounts Committee of the United Kingdom concluded that there was "...no clear difference..." between the government's Export Credits Guarantee Department (ECGD) and commercial banks. The study explained that "...their objectives differ, but in essence, not their prospects of recoverability. The prudence concept of accounting requires the ECGD to recognize the potential losses on sovereign exposure in the form of provisions in the accounts. The best available measure of such losses is provided by the Bank of England's matrix". (The Bank of England's matrix is the U.K. version of the Canadian Superintendent of Financial Institutions' rules.)

2.49 Accordingly, one method of determining the risk of loss on sovereign debts would be to use the valuation guidelines developed by regulatory agencies of national governments for commercial banks. In Canada, the rules developed by the Superintendent of Financial Institutions provide for the risk of non-payment by requiring that a valuation allowance be established of between 35 percent and 45 percent of loans receivable from countries experiencing repayment difficulties. They also provide for accrual of interest to cease where countries are significantly in arrears. Sound accounting practice requires that interest revenue should not be accrued when the ultimate collectability of amounts receivable is not reasonably assured.

2.50 Another method of valuing loans by commercial banks to sovereign nations, which could be used, is by reference to prices in what is called the secondary market for foreign country debts owed to commercial banks. Banks buy and sell in this market to rearrange their holdings of sovereign loans receivable. The secondary market is relatively small compared with other financial markets and does not deal in sovereign-to-sovereign debts. It does, however, assign a value to the risk associated with amounts owed to commercial banks by countries experiencing repayment difficulties.

2.51 As explained in Note 13 to the financial statements, the government believes that payment delays on amounts receivable from sovereign nations are not necessarily indicative of a future loss requiring a valuation allowance (emphasis added). This may be so, but the individual circumstances of each country must be looked at separately. There may be situations where payment delays do indicate future losses. The government does not necessarily receive preferential treatment.

2.52 Moreover, history shows that defaults on sovereign debts do cause real losses. The debt crises of the 1870s, 1890s and 1930s were quite similar to the situation faced today. Although outright repudiation by countries was relatively infrequent, sovereign debtors often sought relief from external debts through complete or partial suspension of repayments followed by renegotiation of the terms and conditions of their loans. In order to settle the defaults, creditors often had to reduce interest rates, reduce the nominal value of the defaulted bonds, or both. In other words, defaults caused real losses.

2.53 Recent proposals to ease the financial burden of external debts on countries experiencing repayment difficulties are strikingly similar. They call for reductions in interest rates and/or reductions in the nominal value of loans and/or extended grace periods. Even the International Monetary Fund and the World Bank -- two of the largest sovereign lenders -- recognize the risk of loss on sovereign debts in their published financial reports.

2.54 I believe that an appropriate allowance for Canadian Wheat Board borrowings should be recorded in the Government's financial statements. There is no simple right answer for the amount of sovereign debt risk to be recognized in this manner. But prudence requires that some reasonable amount be included in the government's financial statements to keep them from being misleading. Clearly, with CWB's receivables in arrears and being rescheduled, there is a very real risk that amounts owing to the Board will ultimately not be repaid. Even if amounts due were ultimately to be repaid, there is the risk of costs associated with repayment delays. And there is the risk of impairment in the present value of amounts owing from what may become virtually "perpetual renegotiation".

2.55 Our analysis indicates that the allowance could range from $1.5 billion to $2.0 billion. In my judgment, the government should record an allowance of at least $1.5 billion. If this were done, reported liabilities and the accumulated deficit would be increased by at least $1.5 billion ($1.3 billion in 1988).

2.56 In saying this, I am not in any way suggesting that CWB should write off its accounts receivable from debtor countries. Sound collection practices must prevail if public assets are to be protected. An allowance for loss on sovereign debts can be recorded in the government's financial statements, without naming specific sovereign debtors. There is no reason why recording such an allowance should in any way impair collection of amounts due. The government is clearly at risk for at least $1.5 billion in borrowings by the CWB that it has guaranteed, and the government's summary financial statements should reflect this reality.

Reservation 2: Failure to Include Crown Corporations in the Government Reporting Entity

In my judgment, the government's financial statements are incomplete. They include government activities of departments, but they do not include government activities of Crown corporations. The government is bigger, and its activities more diverse, than the statements now reveal.

2.57 Although disclosure is now provided in Note 8, the assets, liabilities, revenues and expenditures reported in the separate financial statements of Crown corporations are excluded from the financial statements of the Government of Canada as described in Note

1(i). As a result, I believe that the government's financial statements do not provide a comprehensive and complete summary of the full nature and extent of the financial affairs and resources for which the government is responsible. As of 31 March 1989, the net investment in Crown corporations whose financial statements are excluded from the government reporting entity amounted to approximately $19 billion or about 44 percent of the government's total financial assets.

2.58 In November 1988, PSAAC issued Accounting Statement 4, *Defining the Government Reporting Entity*. This Statement recommended an approach to accounting for government organizations that, if implemented, would make the government's financial statements more comprehensive and complete. If this approach were taken, the financial statements of government-owned corporations that are non-commercial in nature, such as the Canadian Broadcasting Corporation and the Canada Council, would be "consolidated" into the government's financial statements. This means that their assets, liabilities, revenues and expenditures would be added, on a line-by-line basis, to the assets, liabilities, revenues and expenditures of government departments and agencies. Transactions and account balances between these corporations and departments and agencies would be eliminated.

2.59 Government-owned corporations that are commercial in nature, such as Petro-Canada and the Canadian National Railway System, would be included in the government reporting entity on what is known as the "modified equity" basis of accounting. This would mean that the government's investment in commercial Crown corporations would be increased by the government's share of corporate net profits (decreased by corporate net losses), with a corresponding increase (decrease) in its non-tax revenues. Corporate assets, liabilities, revenues and expenditures would not be added to those of departments and agencies on a line-by-line basis as in "consolidation".

2.60 The exclusion of Crown corporations from the government reporting entity has a significant effect on the government's reported financial position and results of operations. Note 8 to the government's financial statements discloses what the statements would look like if prepared as recommended in Accounting Statement 4.

2.61 The figures in Note 8 do not include provision for sovereign debt risk for either the Canadian Wheat Board (CWB) or the Export Development Corporation (EDC). The need for a provision in respect of CWB is discussed in paragraphs 2.41 through 2.56 EDC is discussed in Chapter 4 of this report (paragraphs 4.17 to 4.19) and also in my audit opinion of the Corporation's 1988 financial statements reproduced in Volume III of the Public Accounts of Canada.

Reservation 3: Unrecorded Liabilities

This reservation concerns unrecorded employee pension liabilities. Basic pension benefits are fully provided for in the government's financial statements, but indexed benefits are not. In my view, an additional liability for employee pensions should be included in the government's statements.

2.62 The government has defined liabilities as financial obligations to outside organizations and individuals, resulting from events and transactions recorded as of the closing date (31 March). However, in accordance with the accounting policy stated in Note 1(v), and as described in Note 12, financial obligations related to the indexing provisions of employee pension plans (including those of the public service, the Canadian forces, the Royal Canadian Mounted Police, Members of Parliament and judges) have not been fully recorded. I believe they should be.

2.63 Although Note 12 is informative, it does not change the fact that, until the government adjusts the financial statements to reflect an additional liability for pension indexing, the burden is on the reader to do so. I consider this both undesirable and unfair. A reader unfamiliar with financial statements may get quite a different picture than a reader with more experience.

2.64 Government officials have advised me that they will record an appropriate liability for indexing when revised employee pension legislation becomes law. At the date of signing my opinion on the government's financial statements, this revised legislation had not been presented to the House of Commons.

2.65 In November 1988, PSAAC issued Accounting Statement 5, *Accounting for Employee Pension Obligations in Government Financial Statements*. This Statement recommended an approach to accounting for employee pension obligations that, if implemented by the government, would result in financial obligations in respect of indexing being fully recorded in the government's financial statements. Implementation of these recommendations would allow me to delete Reservation 3 from my audit opinion on the government's statements.

The Role of the Public Accounts of Canada

Important features of the Canadian system of governing depend in part on the availability of good financial information. The Public Accounts are a major source of annually reported financial information.

2.66 The features of the Canadian system of governing that depend in part on the availability of good financial information are:

- consent of the governed;
- an executive entrusted with great powers;
- imposed limits on the executive's use of its powers; and
- oversight of executive actions.

2.67 Government in Canada is based on consent, formally given by representatives in Parliament through the annual appropriation of supply, approval in principle of the Budget and passage of specific legislative proposals. Information on the intended benefits, costs and financial effects of government proposals is needed before Parliament gives its consent. Subsequently, periodic reporting of financial information is needed to compare actual costs, tax burdens and other financial effects with those intended and for which consent was given.

2.68 The system in Canada provides for a strong executive entrusted with great power. The historical reasons for a strong executive are several, including the belief that legislation cannot be formulated to foresee every eventuality; consequently, the executive is trusted to exercise discretion in the application of the laws. Reports of the actual costs and financial effects of government activities are needed to assess whether, from a financial point of view, executive discretion was appropriately exercised.

2.69 Limits on the use of executive authority are a constitutional strategy to protect individuals' liberty from abuse by the powers of the state. Some limits are financial (for example, the system of parliamentary appropriation) and financial records are needed to show whether the executive has complied. Another important limit is jurisdiction; for example, the National Parole Board has sole authority to decide who is released on parole. The practice of granting separate appropriations by department or agency facilitates the control imposed by jurisdictional limits and promotes financial accountability of ministers and public service managers.

2.70 The oversight of the executive in Canada is performed by parliamentarians, the public and interest groups. Parliamentary oversight is as extensive as Members of Parliament make it. Some oversight is accomplished through the news media. The possibility of review helps deter behaviour such as unfairness, fraud, waste, extravagance, embezzlement and misappropriation.

2.71 In the early days of Confederation, protection of the taxpayers' purse was accomplished by publishing the detailed records of financial transactions. These detailed publications evolved into the present-day Public Accounts. Modern government is much larger and more complicated. Publishing financial information at a level of detail comparable to what was published 50 or 100 years ago is not practical; there is a need to be selective in what is published. The government should continue taking the initiative to provide in the Public Accounts basic information that will help the system of governing operate properly. But Parliament must also demand good information.

2.72 A unique opportunity to improve the Public Accounts and related financial information is now developing. The electronic information age has arrived. Its possible effects on the government's 20 year old central accounting and reporting systems, and on departmental systems, are now being studied by central agencies. The government is identifying and pursuing opportunities for improvement at a rapid pace. Parliamentarians can have a voice in these deliberations.

The Need for a Concise Annual Financial Report

Publication of a comprehensive but concise annual financial report, similar to annual reports published by corporations in the private sector, would help parliamentarians and others obtain a complete picture of government without getting buried in massive amounts of detail.

2.73 In 1986, the results of the two-year *Federal Government Reporting Study* (FGRS) were published. FGRS was a research project undertaken jointly by my Office and the United States General Accounting Office. Its purpose was to identify the financial information users need to have about federal governments. The results of the study have been provided to Members of Parliament, the government and PSAAC for its consideration. Copies of the reports on FGRS are available from my Office.

2.74 One question we dealt with in FGRS was how the government's annual financial statements should be communicated. At present, the financial statements are presented in the Public Accounts of Canada, a three-volume set of documents of massive proportions. Users found this presentation cumbersome and difficult to work with. They called for a simpler, more focussed approach to presenting the government's overall numbers. And they wanted some context for the numbers in plain, non-technical language.

2.75 The prevailing view of user respondents was that a comprehensive but concise annual financial report by the federal government would be extremely valuable. They wanted such a report to provide a broad picture and a more complete understanding of the government's activities and resulting financial position and to serve as a key to the more detailed information the government provides in other financial documents.

2.76 Besides basic financial information, such as the government's assets, liabilities, revenues, expenses, deficit and borrowing requirements, most users wanted an annual report to contain other information that would increase their understanding of these indicators. Supplementary information often requested included data on tax expenditures, common measures of the performance of the economy, the effects of inflation, regional breakdowns of revenues and expenses and government employment. Users recognized that such information can be presented in an annual financial report only in a highly summarized format. Nevertheless, they wanted such summary information included, along with references that would allow them to find detailed information on matters they might want to examine further.

2.77 Many users also thought graphs and charts would allow information to be captured quickly and communicated easily. They wanted the charts to provide data for 10 years, where possible; numerical values should also be included to facilitate analysis of trends.

2.78 Since the publication of FGRS, I have been pleased to observe that the government has taken a number of steps to improve the way in which it communicates summary information to users. In 1987, Section 1 of Volume I of the Public Accounts of Canada was completely redone. The section now includes a financial overview containing tables, charts and explanatory narrative, together with more detailed supplementary information. Where possible, data are presented on a comparative basis for 10 years. Topics covered include the deficit and net debt, factors affecting the deficit, and factors affecting financial requirements. Public Accounts Volume I has also been reduced in size. Information not directly related to the government's summary financial statements has been moved to Volume II. With additional work, Volume I of the Public Accounts might well become the sort of concise annual financial report that users need.

In its Eighth Report of 30 June 1987, the Public Accounts Committee endorsed "... the need for a succinct annual financial report for parliamentarians and other users of government financial information".

2.79 In addition, the Department of Finance continues to publish two four-page documents entitled *The Fiscal Monitor* and *The Economy in Brief*. These quarterly publications are attractively presented and contain tables, charts and text designed to help users obtain a complete picture, without getting buried in massive amounts of detail.

2.80 In April 1989, the Department of Finance also published a highly informative financial overview, entitled *Where Your Tax Dollars Go*. This new document summarizes and explains federal spending, with a primary focus on who received federal funds.

2.81 I encourage the government to continue improving the presentation of summary information to users.

The Need for More Consistency

More consistency in accounting and classification practices within the Public Accounts would make it easier to compare actual with forecast results and to move between summary-level and detailed information.

2.82 The Budget is prepared on one basis of accounting while the Main Estimates are prepared on another basis. The Budget also includes reserves for Supplementary Estimates net of lapses. There is a lack of clear, obvious links between similar information in these two documents. For example, Table 4.4 from the 1989-90 Budget Fiscal Plan and Table 4.1 from Part I of the 1989-90 Estimates both present expenditures by type of payment (see Exhibit 2.1). The only amount in the 1989-90 columns that is the same in both tables is $39.4 billion of projected public debt charges. The 1989-90 projected expenditure totals differ by $12 billion. This difference is analyzed in Table 2.2 of Part I of the 1989-90 Estimates.

2.83 The differences in accounting between Budget and Estimates are reflected in the Public Accounts. Detailed information in Volume II of the Public Accounts often cannot be easily tied in to the government's summary financial statements in Volume I. Consider the question: What was the effect of government activities related to employment and insurance on the deficit in 1987-88? The possible answers are shown in Exhibit 2.2. Depending on one's knowledge of government organization and accounting expertise, the two possible answers differ by almost $2 billion. The correct answer -- $2.447 billion -- could be determined only by someone who knows the composition of the government's valuation allowances. This information is not available from published sources.

2.84 In paragraphs 2.66 through 2.72, we set out the uses of financial information in the Canadian system of governing: it is the basis for consent to executive action; for imposing financial limits; and for oversight by Parliament and the public. These uses can be better served if financial information is comprehensive in its coverage of government activities and understandable to those who need to use it.

2.85 As part of the 1986 Federal Government Reporting Study (see paragraphs 2.73 through 2.81), we consulted Members of Parliament on their financial information needs. The study report summarized the characteristics such information should possess:

> It needs to be presented in a way that allows the Member to move easily from summary-level data to the more detailed accounting of the particular issue of concern. Information should allow first an overview and then a more detailed analysis of individual departments' expenditures and performance. This information requirement extends to the review of the government's Budget, the Estimates of the various departments and agencies, and the annual reports of the various government-owned corporations. In carrying out their parliamentary activities, Canadian Members want to be able to compare reported actual results with forecasts in the Budget and Estimates (requests for spending authority) and with spending and borrowing limits set by acts of Parliament. It is essential, therefore, that there be consistency in classification and format among the basic financial reports of the government.

2.86 In our view, financial information in the Public Accounts, Budget and Estimates does not have the characteristics that Members believed to be essential to their activities. Inconsistencies in accounting and classification practices make it difficult to compare actual results with forecast results or to move easily between summary-level data and detailed program accounting data.

2.87 Government accounting, like all accounting, is continually evolving. Major trends in government summary financial reporting over the last 20 years have been:

- the elimination of internal transactions and balances so as to report in terms of transactions with outside parties;
- the grossing up of amounts of revenues netted against expenditures and of expenditures netted against revenues;
- a more complete reporting of the liabilities of the government; and
- the provision of allowances to reduce the recorded values of financial assets to estimated amounts realizable.

An illustration of inconsistent accounting and classification.

The 1989 Budget, Table 4.4

Budgetary Expenditures by Type of Payment

	1987-88(1)	1988-89(2)	1989-90(3)	1990-91(3)
	(millions of dollars)			
A. Transfers to persons: of which	28,783	30,025	32,585	34,360
Payments under the unemployment insurance program	10,487	10,925	11,930	12,725
Old age security benefits	14,349	15,280	16,395	17,645
Family allowances	2,564	2,600	2,610	2,645
B. Transfers to other levels of government: of which	21,519	24,340	24,010	25,180
Established Programs Financing	8,800	8,905	9,140	9,660
Equalization	6,386	7,300	7,295	7,680
Canada Assistance Plan	4,246	4,595	4,780	5,000
C. Major subsidies and transfers	11,477	11,220	10,515	10,230
D. Major payments to Crown corporations	5,784	4,410	4,740	4,685
E. Defence	10,769	11,075	11,210	11,995
F. Official Development Assistance	2,599	2,780	2,445	2,660
G. Operations of government	15,577	16,150	16,975	17,545
H. Reserves net of lapse	-	-	1,020	2,325
I. Program expenditures	96,507	100,000	103,500	108,980
J. Public debt charges	29,028	33,000	39,400	39,820
K. Total budgetary expenditures	125,535	133,000	142,900	148,800

(1) Actual (2) Estimate (3) Forecast

The 1989-90 Estimates, Part I, Table 4.1

Budgetary Main Estimates by Type of Payment

($ millions)	1988-89 Main Estimates	1989-90 Main Estimates	Change	Percentage change
Transfer payments				
To other levels of government	22,665	23,896	1,231	5.4
To persons	22,329	23,691	1,362	6.1
Subsidies	2,038	2,363	325	15.9
Other	9,748	9,788	40	0.4
Sub-total: transfer payments	56,780	59,738	2,958	5.2
Public debt charges	32,055	39,400	7,345	22.9
Payments to Crown corporations	4,528	4,805	277	6.1
Operating and capital expenditures				
National Defence	11,200	11,340	140	1.3
All other departments and agencies	14,803	15,705	902	6.1
Sub-total operating and capital	26,003	27,045	1,042	4.0
Total	119,366	130,988	11,622	9.7

Exhibit 2.1

2.88 The changes in accounting policies and practices have resulted in substantial improvement to the completeness and comprehensiveness of reporting in the government's summary financial statements and in the Budget. However, many of the changes were implemented by making accounting adjustments only at the summary level. The accounting changes have not been implemented at the program level where the departmental Estimates are prepared. The Estimates and program-level reports in the Public Accounts continue to follow accounting practices developed for reporting on the use of appropriation authority. The government abandoned these practices for purposes of summary reporting because they were considered to be inappropriate.

The impact of some activities on the deficit can be determined only by an expert using unpublished financial information.

ILLUSTRATION OF THE DIFFICULTY OF LINKING DETAILED AND SUMMARY INFORMATION IN THE PUBLIC ACCOUNTS

Question: How did the employment and insurance activities affect the 1987-88 deficit?

Possible Answers:

	$ millions
1. Answer based on information reported at the program level in Volume II, Part I of the Public Accounts	
Program expenditures	4,365
Program revenues	13
Impact on deficit	4,352
2. Answer based on adjusting program level data of answer 1 to consolidate the Unemployment Insurance Account, using information reported in Tables 5 and 6 of Volume II, Part I	
Consolidated program expenditures	12,864
Consolidated program revenues	10,438
Impact on deficit	2,426
3. Correct answer, adjusting answer 2 taking into account unpublished information on the composition of the provision for valuation of statutory payables	
Consolidated program expenditures	12,885
Consolidated program revenues	10,438
Impact on deficit	2,447

Exhibit 2.2

2.89 The complexity can be reduced by carrying down to the program level the adjustments now made only at the summary level. There would then be a single definition of expenditure used for summary reporting, for preparing Estimates and for reporting expenditures at the program level. There would be a corresponding single definition of revenue. This accounting change would eliminate the current difficulty in relating detailed program information to summary-level information. It would also reduce the complexity of tables in the Public Accounts.

2.90 The government should prepare its spending Estimates and account for and report its revenues and expenditures at the program level in accordance with the accounting policies and practices it uses for summary reporting.

2.91 The accounting changes over the last 20 years reflect a trend toward accounting for revenues and expenditures in terms of gross transactions with outside parties. The gross amount of revenues and expenditures is needed to understand the full magnitude of government financial activity and its impact on the economy. It is also needed to fully report on the use made of revenue and spending authorities.

2.92 Current Budget presentations do not fully gross up all the revenues from or expenditures to outside parties. In excess of $2 billion of tax and non-tax revenues are netted against expenditures. As disclosed in Note 4 to the government's financial statements, a further $2 billion of expenditures, in the form of refundable tax credits, are netted against tax revenues. One effect of netting refundable tax credits is that the income tax load on individuals, when compared with that on corporations, is understated by

$2 billion. I have not commented on the practice of netting in a reservation to my opinion on the government's financial statements because it has no effect on the reported deficit for the year. However, if the practice becomes more pervasive, reported revenues and expenditures may become so distorted that a reservation will be required.

2.93 The government should account for and report its revenues and expenditures consistently in terms of gross transactions with outside parties.

3

MAJOR CAPITAL PROJECTS

3

MAJOR CAPITAL PROJECTS

Main Points

3.1 We examined five construction projects having a total value of approximately $650 million. In one case, by the time the project is completed, planning and construction will have taken 16 years; in another, a long-term strategic plan is still not in place, although $375 million has been expended (paragraphs 3.16, 3.54 and 3.55).

3.2 The Department of Public Works (DPW) was directed to purchase a facility at Rigaud, Quebec at a cost of $5 million for a Customs and Excise (C & E) Training College, although it did not meet C & E requirements. Although the original consultants' report stated the property would be adequate to meet C & E needs "with some renovations", the cost of renovations so far has been $35 million (3.22, 3.23 and 3.30).

3.3 The Maurice Lamontagne Institute in Mont Joli Quebec, the estimated cost of which was initially reported to Parliament at $17 million, was built for the Department of Fisheries and Oceans at an approved cost of $48.2 million. The Department estimates the eventual cost to be $56.7 million; we conclude that an additional $20.9 million will be required to complete the facility to its full capabilities, raising the cost to $77 million (3.39, 3.43 and 3.49).

3.4 The Department of Public Works is accountable for the Northwest Highway System and the Department of Indian Affairs and Northern Development (DIAND) is responsible for the Northern Roads Program. In 1973, Treasury Board directed that the Northwest Highway System and the inter-territorial roads under the Northern Roads Program be turned over to British Columbia, Yukon, and the Northwest Territories. This divestiture has not taken place (3.55).

3.5 DIAND has reached agreement in principle with the Yukon and Northwest Territories Governments to transfer the remainder of the Northern Roads Program, at annual funding levels of $8.1 million and $9.4 million respectively, without obtaining Cabinet's approval for a framework to transfer responsibilities for roads (3.50).

3.6 We found the capital projects of the Rideau Canal and Trent-Severn Waterway of the Canadian Parks Service were well managed in accordance with our criteria for due regard to economy and efficiency. The Bassano Dam project met the audit criteria during the implementation phase (3.65 and 3.19).

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MAJOR CAPITAL PROJECTS

Introduction

We examined five construction projects

3.7 As part of the Office's continuing examination of capital acquisitions by federal departments and agencies, we examined five construction projects with a total value of about $650 million: the Bassano Dam in Alberta; the Customs and Excise Training College at Rigaud, Quebec; the Maurice Lamontagne Institute, Mont Joli, Quebec; the Northwest Highway System and Northern Roads Program; and the Rideau Canal and Trent-Severn Waterway. These projects are representative of departments' efforts to acquire new facilities to provide accommodation and service.

Audit Scope

Progress of each project

3.8 We examined each project using criteria developed by our Office, approved by the Public Accounts Committee, and agreed to by the departments concerned. We assessed the progress of each project from the time departments had identified the need for construction up to the time of our audit.

Planning and management systems

3.9 We focussed on how departments plan capital projects as well as the systems and practices they use to manage them. We also examined how the projects were related to departmental plans and objectives.

Contracts

3.10 We also looked at contracts to assess whether officials in the departments and the service agency, the Department of Public Works (DPW), had followed departmental and Treasury Board direction in developing appropriate contractual arrangements for each project.

3.11 For those projects that had reached the commissioning phase (the phase in which the equipment or construction is turned over to the Crown), we assessed whether departments had received the equipment or buildings for which they had contracted.

Audit Findings

Planning not significantly improved

3.12 We found no evidence that departmental and agency planning had improved significantly over previous years. One project, the Bassano Dam rehabilitation, will have taken over 16 years from the original planning to project completion. During the planning period the estimated cost of the project escalated from $5 million to $17.2 million. In the Northwest Highway System, long- term strategic plans for both highway construction and divestiture of highways and roads to British Columbia and the Yukon Territory were still not in place.

Needs definition and options analysis flawed

We examined five construction projects with a total value of about $650 million.

3.13 In the case of the Maurice Lamontagne Institute, the Department of Fisheries and Oceans had been directed to build the facility and, operating under the pressures of the Special Recovery Capital Projects Program (SCRPP), did not have time to carry out a needs or options analysis. The cost, reported to Parliament in 1983 at $17 million, is now projected at $56.7 million. With the additional components that, in our view, are necessary to complete the project, the cost will eventually rise to $77 million. For the Rigaud project, Customs and Excise did not review its options when a major change occurred that could have had a significant impact on the need for a project of that size.

Two projects ran into difficulties

3.14 The Rigaud Training College for Customs and Excise ran into difficulties during the implementation phase, due largely to inadequate evaluation of the facility's condition when it was purchased. In addition, we noted that there were no standards governing the construction of residential facilities. In the case of the Maurice Lamontagne Institute, we concluded that an additional $20.9 million will be required before the facility can be used to its full potential.

Some well-managed projects

3.15 We also noted two capital programs that were well managed in accordance with our criteria: the Rideau Canal and the Trent-Severn Waterway. In addition, once the Bassano Dam project reached the implementation stage it was managed with due regard for economy and efficiency.

Case Studies

Case Study 1: Rehabilitation of the Bassano Dam, Bassano, Alberta

Long delays but well managed once under way

3.16 Under an agreement between the federal government and the government of Alberta, signed in 1973, the Prairie Farm Rehabilitation Administration was directed to undertake the rehabilitation of several irrigation works in the Province. The federal government initially committed support totalling $26.2 million, not including the value of property it transferred to Alberta, estimated at $2 million. $16.5 million was identified as the

Bassano Dam Alberta; delayed by over 10 years; costs increased 300% (see paragraphs 3.16 to 3.19).

estimated cost to rehabilitate four irrigation works, including the dam at Bassano, originally built in 1914. The agreement called for the rehabilitation projects to be completed within five years; the Department of Regional and Economic Expansion estimated that the works at the Bassano Dam would cost $5 million.

3.17 The Bassano Dam project was delayed for six years while land claims with the neighbouring Blackfoot Indian Band were dealt with, during which time construction costs escalated for reasons beyond the control of the PFRA. In 1984, PFRA was authorized to start the project, expected to take two years at an estimated cost of $17.2 million.

3.18 The project was further delayed by problems encountered in rehabilitating a working structure over 70 years old for which original design drawings were unreliable. As a result, the dam's rehabilitation is now scheduled for completion in 1989-90. The anticipated cost of the project is about $15.5 million, about 10 percent below the 1984 estimate.

3.19 We have examined the implementation phase of the Bassano Dam project from all aspects, and consider it to have been well managed by PFRA in accordance with our criteria.

Case Study 2: Training College, Rigaud

A catalogue of problems and delays

3.20 The Department of National Revenue, Customs and Excise (C&E) had determined by 1976 that it needed a training college for customs and excise officers. At the same time the Taxation Branch of the Department was considering a "Centre for Career Development" which could be located with the proposed college.

3.21 C & E was given approval in principle, in June 1976, to build a college at a location that would support the government's decentralization policy. With Taxation's requirements at that time, the combined capacity of the facility would be about 450 residential rooms.

3.22 The Department of Public Works (DPW) was directed to buy the College St. Viateur at Rigaud at a cost of $5 million to meet the C & E and Taxation requirements, even though C & E had previously indicated that the location met none of the criteria for departmental requirements, or for the government's decentralization policy. Following the purchase, preliminary repairs were undertaken to enable the college to commence operating immediately. Taxation withdrew from the project in November 1978, but Customs and Excise indicated that its training requirements would grow, in the longer term, enough to take up the vacated capacity.

3.23 In 1984 the Department of Public Works started the main renovation project, with an estimated total cost of $34,986,000 and a scheduled completion date of October 1987. Completion is now scheduled for the fall of 1989.

3.24 We examined the process followed by the Department of National Revenue (C&E) in determining the need for a college and concluded that the initial needs definition phase had been performed satisfactorily. However, when Taxation withdrew in 1978, no re-examination of need was undertaken, even though up to that point C & E had been expected to require only half the facility's total capacity.

3.25 Over the three years before the contract for the main renovations was awarded in June 1986, C & E training days achieved were about 60 percent of those planned. We noted that in 1981 when cost increases were reported and in October 1985, when the results of tenders indicated that a significant cost reduction would be necessary to keep within the budget, Customs and Excise did not re-examine alternatives in light of the fact that its planned training program had apparently overstated its needs.

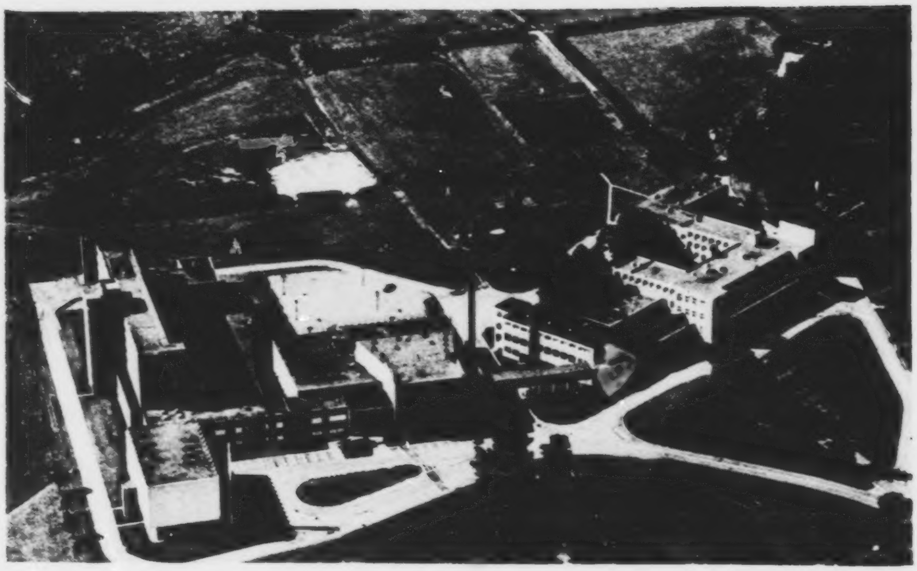
3.26 In summary, when construction started in 1986, it was to meet needs established in 1976 and not re-examined since then.

3.27 We examined the options analysis undertaken in 1976 and are satisfied that it was adequate. We recognize that once the property had been purchased, the options were restricted to the extent and design of the work needed to make the facility acceptable as a training college. In our opinion, however, had the Department examined other options before seeking Effective Project Approval from the Treasury Board, it could have determined and advised the Board whether a smaller project with provision for future expansion could have been completed sooner and more economically.

3.28 The Department has informed us that due to recent changes in compulsory course requirements for Customs Inspectors, and with anticipated legislative changes likely to have a significant impact on the Excise Branch, there may well be a requirement for the full facility.

3.29 We examined the process by which the Department of Public Works (DPW) and the Department of National Revenue (C&E) estimated the total cost of the project. We found that both Departments followed appropriate procedures.

3.30 Before acquiring the property in 1977, DPW engaged two consultants at $10,000 each. Their preliminary analysis indicated that, with some renovations, the property would



The Customs and Excise College, Rigaud, Quebec, before renovation (see paragraphs 3.21 to 3.38).

be adequate as a training college for Customs and Excise and Taxation. (We noted, however, that there were no criteria for training institutions or precise accommodation standards for either department). In 1978, the same architectural consultants were engaged to prepare the studies for the preliminary renovation work, which would allow the College to begin operating. In 1980 they were again appointed to conduct the preliminary studies for the main renovation project and, having so far demonstrated satisfactory performance, were engaged jointly with another firm to undertake the main design work and site supervision in 1983.

3.31 In our opinion, for a project of this nature and scope, the initial contracts did not provide enough latitude for a realistic evaluation before the decision to proceed. The full scope and criteria for technical training were not provided until the consulting contract for the main work was signed in May 1983. By then approximately $8 million had already been spent to buy the property, and to complete emergency work and sufficient renovation to maintain the security of the building and permit limited operation of the College. This amount was in addition to the cost of the main renovation project -- about $35 million.

3.32 DPW followed Treasury Board and departmental directives in seeking an architectural consultant for the project, but was directed to engage a second consultant to work jointly with the recommended firm. During the main design phase, the joint consultants were often late and demonstrated less than full co-operation with the Department.

3.33 In March 1980 Customs and Excise started limited operation of the training college, which continued throughout the renovations, a condition the consultants said was one of the constraints to delivering the project on time.

3.34 In any other renovation project, the option of occupying the premises during construction should be carefully evaluated.

3.35 In August 1985 tenders were called for the main renovation package. The lowest valid tender at about $24 million exceeded DPW estimates by almost $5 million, or 25 percent. As a result, a cost reduction exercise was undertaken to ensure that the project would remain within the approved TB budget and a total of $4.6 million was cut from the project. C & E expressed some concern over the impact these cuts would have on its training program, but nevertheless concurred with the decision. On completion of the cost reduction exercise a new tender call was issued and a valid tender for the main renovation work was accepted in June 1986. This time, the tenders received were within DPW's estimates. To cover the additional work needed due in part to site conditions and the increased time spent to prepare for the second tender call, the consultants' fees were increased by over $1 million.

3.36 DPW's cost estimates before the two tender calls had been based on consultants' advice, which we evaluated in the light of the results of the two calls. The consultants had advised that the notable difference between the estimate and the result of the first tender call was due to "unusual market conditions" and the difficulties inherent in a project of this complexity. We were unable to confirm the basis for this advice. As a consequence, we conclude that the Department of Public Works was not kept fully informed.

3.37 Work began on the main renovation package in late 1986, with completion scheduled for October 1988. Changing requirements and unexpected conditions in the old buildings have combined to delay the project by almost a year and to increase the cost of the contract by some $3.1 million. These increased costs have been the result of over 380 change orders. In our opinion, some of these unexpected problems could have been avoided had there been an adequate examination and analysis of the buildings and had the client's needs been adequately defined prior to the start of design work.

3.38 Thirteen years after the initial requirements were identified, the project has been kept within the Treasury Board approved budget, but only by completing a significant cost reduction exercise, which reduced the standard of quality of the facility. The project is now over two years late.

Case Study 3: Maurice Lamontagne Institute, Mont Joli, Quebec

A story of escalating costs

3.39 In 1983, the Department of Fisheries and Oceans (DFO) was directed, under the Special Recovery Capital Projects Program (SRCPP), to build a marine sciences research institute near Mont Joli, Quebec. The institute would accommodate research scientists and the cost was reported to Parliament in the 1984 Main Estimates at $17 million.

3.40 Because the Department was directed to establish a world-class facility of a given size and in a given location and because of time constraints, neither a full needs analysis nor a full options analysis was undertaken.

3.41 The exigencies of the SRCPP were such that DFO and the Department of Public Works (DPW) were under severe time pressures to meet SRCPP objectives. In our opinion DPW and DFO managed the definition stage well in trying to meet these requirements. The Department of Public Works followed departmental and Treasury Board directives in selecting the design consultants and the contractors, but was told which design consultant to engage. As a result, an architectural firm was engaged whose design proposal and capability had been ranked second and whose tendered price was over $200,000 more than the lowest bidder, whose proposal had been ranked first.

3.42 In attempting to meet the construction timetable, the Department of Public Works went to tender before completing a thorough cost estimate of all elements of the project, and before all design documents were completed. Furthermore, to comply with SRCPP guidelines to reduce the time for construction and to allow more contractors to participate, the project was broken down into several small phases or construction lots. Work costing $2.4 million was eventually added to the various construction contracts to accommodate unforeseen site or design conditions; about $400,000 of this, the Department of Public Works estimates, was due to time pressures. DFO calculated that costs related to the remote location selected for the project would amount to about 10 percent of the construction costs. In our opinion, a similar project undertaken without the pressures of the SRCPP and in a less remote location could have been built for as much as $5.2 million less.

3.43 The project was approved at an initial estimated total cost of $44 million. Additional costs have increased the approved total to $48.2 million. However, the Department of Fisheries and Oceans estimates that the cost of the project will be $56.7 million, excluding both a computer and the second phase of the harbour facilities, which the Treasury Board had been advised would be addressed in future submissions. The additional $8.5 million is to cover expected additional work to complete designs (at $6 million) that were part of the original scope of the project, and new waste water treatment facilities which have been necessitated by changes in environmental regulations.

3.44 Regulations governing the treatment of waste water were changed after construction had been completed. Until the facilities to meet the new regulations are constructed, at an estimated cost of $2.5 million, domestic sewage is given primary treatment, and liquid chemical and biological wastes are only diluted before being emptied into the St. Lawrence River.

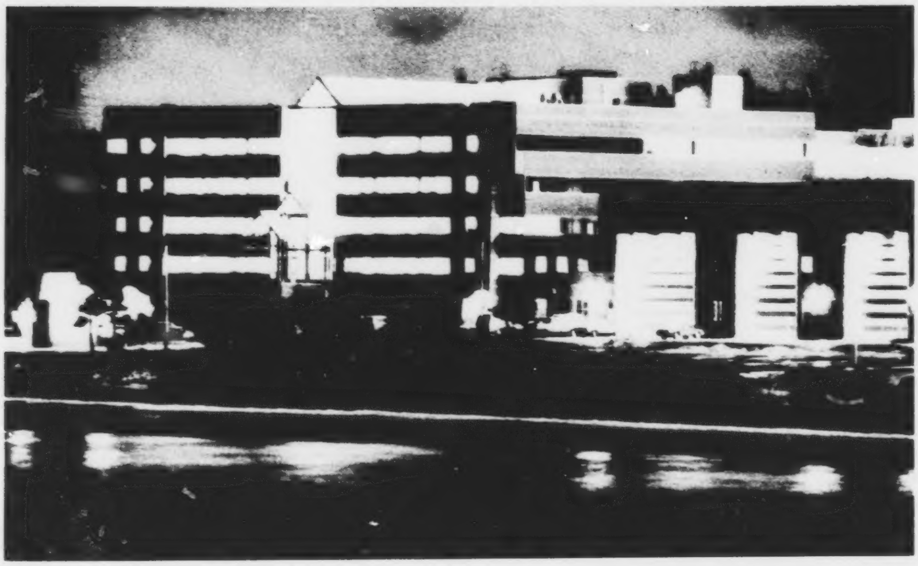
3.45 A central computer necessary to meet the scientific computing requirements of the institute was identified in the original TB submission but not costed. A separate submission was to be made for the computer and the Department now estimates the cost of providing this essential facility to be $5.6 million.

3.46 As part of the project so far approved, DFO has constructed an approach jetty costing $8 million. The Department expects that this jetty can be used only about 25 percent of the time that the St. Lawrence River is ice-free. An additional $13 million will be required to construct a breakwater if the jetty and harbour are to be used more often. We consider that the Department has not fully justified its requirement for the harbour, and decisions still need to be made on the future of the harbour.

3.47 Additional construction of minor works, at a total cost of $2.3 million, has been identified by the Department as "desirable but not essential".

3.48 In addition to the $8.5 million the Department estimates it will need to complete the project, we have identified a further $20.9 million ($5.6 million for the computer; $13 million for phase II of the harbour; and $2.3 million for "desirable, but not essential" minor works). The first two items were identified in the original Treasury Board submission as requests for future submissions but were not fully costed.

Initially reported as $17 million, we estimate the final amount will be $77 million (see paragraph 3.49).



3.49 In summary, the Department was directed to undertake the project with a cost originally identified to Parliament at $17 million and subsequently approved by Treasury Board at $48.2 million. The Department expects the project to cost $56.7 million, but its estimates do not include the costs of the additional items, amounting to $20.9 million, described previously. In our view, these elements are needed before the project meets the standard originally considered appropriate for a world-class facility. We are aware that the Treasury Board was advised of further submissions that would cover the additional items, but we have calculated that completing it to meet the full scope of its capabilities as originally approved will bring the cost to over $77 million, or nearly $30 million more than originally estimated.

Case Study 4: Northwest Highway System and Northern Roads Program

Lack of plans, funds and other difficulties delay divestiture proceedings

3.50 In 1958, the federal government approved the Northern Roads Program, currently administered by the Department of Indian Affairs and Northern Development (DIAND), to develop the oil and mineral potential of the Yukon and the Northwest Territories. The program has since been updated to introduce new economic measures designed to encourage economic development by determining, using socio-economic criteria, the construction requirements for a network of permanent highways and roads in the territories.

3.51 In 1964, administration and control of the Northwest Highway System, Haines Road and all property forming part of the Northwest Highway System were transferred to the Department of Public Works (DPW). The Department introduced a policy of gradual highway reconstruction and paving, in areas where traffic volume and accident rates justified the cost of improvements.

3.52 We reviewed management controls and engineering procedures and practices related to the maintenance and construction of nine highway and road systems.

Tractor train (160,000 lbs.) loaded with mineral concentrate on unfinished highway. Delayed divestiture of northern roads has contributed to lack of maintenance and reconstruction (see paragraphs 3.50 to 3.64).

3.53 We also examined the current status of the divestiture of territorial highways and roads initially directed by Treasury Board in 1973.

3.54 From 1980 to 1989 DPW paid $375 million to maintain and reconstruct the Northwest Highway System. DIAND paid $140.2 million between 1981 and 1989 to construct and reconstruct roads under the Northern Roads Program. These expenditures are approximate and do not represent the full cost of constructing and reconstructing the highways and roads.

3.55 In our 1979 audit of DPW highways and roads systems we reported the lack of long-term strategic plans for capital road construction for the Northwest Highway System. These plans have not been developed.

3.56 In 1986, Treasury Board directed that DIAND should seek approval of a capital plan only in the context of a Cabinet-approved framework for the transfer of responsibilities to the Territories. However, DIAND has reached agreement in principle with the Yukon and Northwest Territories Governments to transfer the remainder of the Northern Roads Program, at agreed annual funding levels of $8.1 million and $9.4 million respectively, without obtaining Cabinet approval for a framework to transfer responsibilities for the roads. DIAND is now in the process of seeking Cabinet approval for the transfers at the agreed funding levels. This is the final transfer of the current Northern Roads Program.

3.57 The transfer to the respective governments of responsibilities for roads is delayed because of differences over the wording of the agreements and because responsibilities for funding future roads need to be clarified. DIAND has already transferred its road maintenance responsibilities for both territorial and inter-territorial roads and its construction responsibilities for territorial roads to the territorial governments.

3.58 Notwithstanding a 1973 Treasury Board direction, the Northwest Highway System, and inter-territorial highways and roads under the Northern Roads Program, have not been transferred to British Columbia, Yukon and Northwest Territories.

3.59 Demands by the Province of British Columbia, and conditions under which the Yukon Government has indicated it will accept responsibility for its sections of the Northwest Highway System, have become so complex that divestiture is not likely to occur without major financial concessions by the federal government.

3.60 The lack of long-term strategic plans for capital roads for the Northwest Highway System, providing for realistic funding based on justified social and economic needs, has made it difficult to determine the annual funding levels that are and will be required until the divestitures can be negotiated, to properly maintain and reconstruct the highways and roads at acceptable safety levels and design standards. DPW is presently engaged in an economic review of highway requirements.

3.61 The lack of funds has caused DIAND difficulty in achieving prompt agreement with the Yukon and Northwest Territories Governments on the acceptance of capital road plans and the annual funding levels required for transfer of road responsibilities.

3.62 The current restriction of capital funds for the Northwest Highway System has had an adverse effect on Public Works' ability to meet the conditions laid down by the British Columbia and Yukon governments for divestiture of the highway.

3.63 We noted that $7.3 million for the upgrading of the South Klondike Highway was approved on 19 July 1983 in spite of Treasury Board's concern over the economic viability of the project. Since that time $20.8 million has been expended on reconstruction of this highway with Treasury Board approval.

Payment for work done in error

We examined the capital works of the Rideau Canal and the Trent-Severn Waterway, and found them to be well planned and well managed.

3.64 Our examination of management controls revealed that in November 1983 a payment of $1,227,000 was made to the Yukon Government for work carried out in error on a federal section of the Carcross-Skagway Highway, fourteen months before completion of a Treasury Board-directed audit, to be done as a prerequisite for payment. The payment was approved by Treasury Board, on condition that DIAND formally define its responsibilities for inter-territorial roads with the two territorial governments. This has not yet been done.

Case Study 5: Rideau Canal and Trent-Severn Waterway

Well planned and well managed

3.65 The Rideau Canal and the Trent-Severn Waterway are Heritage Canals operated by the Canadian Parks Service of the Department of the Environment. They each spend approximately $3 million annually on capital projects. We examined all the capital works of the two systems for 1986-87, and in accordance with our criteria for due regard to economy found them to be well planned and managed.

4

AUDIT NOTES

4

AUDIT NOTES

Main Points

4.1 The Audit Notes chapter fulfils a special role in the annual report. Other chapters normally describe the findings of the comprehensive audits we perform in particular departments; or they report audits and studies of issues that relate to government operations as a whole. The Audit Notes chapter brings together in one place individual matters that have come to our attention during our financial audits of the Public Accounts of Canada, Crown corporations and other entities. It is also used to report some individual matters that have come to our attention during the performance of our comprehensive audits.

4.2 Where, in the Auditor General's judgment, these matters are of significance and of a nature that they should be brought to the attention of the House of Commons, the Auditor General Act requires him to include them in his annual report.

4.3 The Audit Notes chapter is, therefore, a compilation of these instances.

4.4 This year's chapter contains a wide range of notes. Three relate to Crown corporations and other entities, and the balance to departmental operations. Several involve large expenditures of public moneys.

4.5 While the notes report matters of significance, they should not be used as a basis for drawing wider conclusions about matters we did not examine.

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AUDIT NOTES

Introduction

4.6 This chapter contains matters of significance that we believe should be drawn to the attention of the House of Commons. They have not been reported elsewhere in the report, but have come to our attention during our audits of the accounts of Canada, Crown corporations and other entities or during the performance of our comprehensive audits.

4.7 Section 7(2) of the Auditor General Act requires the Auditor General to call Parliament's attention to any significant cases where he has observed that:

(a) accounts have not been faithfully and properly maintained or public money has not been fully accounted for or paid, where so required by law, into the Consolidated Revenue Fund;

(b) essential records have not been maintained or the rules and procedures applied have been insufficient to safeguard and control public property, to secure an effective check on the assessment, collection and proper allocation of the revenue and to ensure that expenditures have been made only as authorized,

(c) money has been expended other than for purposes for which it was appropriated by Parliament;

(d) money has been expended without due regard to economy or efficiency; or

(e) satisfactory procedures have not been established to measure and report the effectiveness of programs, where such procedures could appropriately and reasonably be implemented.

The audit notes contain individual matters of significance that the Auditor General is drawing to the attention of the House of Commons.

4.8 Each of the matters of significance reported in this chapter was examined in accordance with generally accepted auditing standards, and accordingly our examinations included such tests and other procedures as we considered necessary in the circumstances. The matters reported should not be used as a basis for drawing conclusions about matters not examined. The instances that we have observed are described in this chapter under the appropriate Crown corporation, department or agency heading.

Observations on Crown Corporations and Other Entities

4.9 The Auditor General is appointed auditor of a number of Crown corporations and other entities, under the Financial Administration Act, individual Acts incorporating specific corporations or by Orders in Council. Details of significant reservations and other matters contained in reports issued to these corporations and entities during the year are set out below. Most of these matters have already been raised in a public forum, but they are reported here for emphasis and for consideration by Parliament.

Government of Canada - The Government has Issued, Without Proper Authority, a Letter of Comfort Guaranteeing $3.7 Billion of the Canadian Wheat Board's Receivables

> In 1972, the Government issued a letter assuring the Canadian Wheat Board (CWB) that its receivables arising from export credit sales of grain were guaranteed by the government in the event of buyer default. To give such a guarantee requires the authority of Parliament, and no such authority has ever been sought. As a result of this letter, the Board has distributed at least $1.5 billion of "surpluses on operations" to producers, and the government has accumulated a contingent liability of up to $3.7 billion. Currently, the Board is carrying $3.2 billion in loans that are troubled.
>
> By failing to seek Parliament's authority to guarantee the Board's receivables, as is explicitly required by section 29 of the Financial Administration Act, the Government has denied Parliament its right of prior approval before commitments are made. This has left Parliament in the situation of being asked to approve an expenditure long after the liability has been incurred and without the opportunity to consider alternative courses of action.

4.10 The Canadian Wheat Board Act (CWBA) gives the Canadian Wheat Board the authority to borrow funds. It also gives the government the authority to guarantee to the Board's creditors repayment of their funds in the event that the Board is unable to repay its borrowings. These guarantees are reviewed regularly on a country and amount specific basis by Cabinet.

4.11 In 1971 the Board became concerned that, in the event that its debtors were to default on their loans, the Board would in turn be unable to pay its obligations. The Board was of the view that the Government was committed to assuming the risk of non-payment by the Board's debtors, and asked that this commitment be expressed formally.

4.12 The Government considered the matter in 1972. To give the assurance that the Board wished would in effect be to guarantee to the Board its receivables in the event one of its debtors were to default. The authority to give such a guarantee can only be given by an Act of Parliament. Documents we reviewed confirm that the Government was fully aware of this. However, a decision was made by Cabinet to have the then Minister for the Canadian Wheat Board write to the Board and assure it that there is no question that the government is liable for the risk of non-payment by the purchaser. The letter was sent on 4 May 1972. The Board is of the view that this letter represents a binding commitment on the government to guarantee its receivables and it cites a recent Federal Court of Appeal decision in its support. This commitment has been reaffirmed on subsequent occasions by Cabinet, most recently in 1987. Despite the fact that the CWBA has been amended on several occasions since 1972, no Parliamentary authority has been sought for this guarantee.

4.13 The CWBA requires that the Board receive payment in full for the grain it has sold before it pays the "surpluses on operations" from these sales to producers. However, in 1979 some of the Board's debtors began to default on their loans. Currently, the Board is carrying $3.2 billion in loans that are troubled, and the value of these loans is, in our opinion, impaired by at least $1.5 billion (see Chapter 2, paragraphs 2.41 to 2.56). Nonetheless, based on this guarantee of its receivables the Board believed that, for all intents and purposes, it had sufficient assurance of receiving "payment in full" that it could proceed with making the distributions of the surpluses on operations to producers.

4.14 The consequences of this are that, under this guarantee issued without proper authority, at least $1.5 billion of surpluses on operations have been distributed to producers and the government has incurred a contingent liability to the Crown of up to $3.7 billion, the amount of the Board's receivables. This has been done without Parliament's authority.

4.15 The Wheat Board's receivables and the accrued interest on them have grown over the years to a very large sum that continues to grow at a rate of several hundred million dollars a year. Sooner or later, Parliament is likely to be asked to authorize payment from the Consolidated Revenue Fund to cover some or all of the payments which would be required under a guarantee of the receivables. By failing to seek Parliament's authority to guarantee the Board's receivables, as is explicitly required by section 29 of the Financial Administration Act, the Government has denied Parliament its right of prior approval before commitments are made. This has left Parliament in the situation of being asked to approve an expenditure long after the liability has been incurred and without the opportunity to consider alternative courses of action.

4.16 We wrote government officials but, at the time of going to press, we did not have a reply. However, there were indications that we might expect corrective action soon. We will continue to monitor the situation.

Export Development Corporation - Inadequate Recognition of Sovereign Risk

> Many lesser developed countries are continuing to experience difficulties in repaying loans as they become due. The auditor's report on the financial statements of the Export Development Corporation (EDC) for the year ended 31 December 1988 was qualified because of a departure from generally accepted accounting principles (GAAP). The Corporation had $4.726 billion in sovereign loans, against which a general allowance for losses of $107.8 million on loans was recorded on the balance sheet. We believe that this allowance is inadequate to recognize the sovereign risk involved.

4.17 In our opinion, loans receivable are overvalued because the Corporation's estimate of the allowance for losses on loans is significantly understated. It therefore does not conform to generally accepted accounting principles. Although the scope of our examination was adequate to arrive at this conclusion, we could not determine the precise magnitude of the overstatement of loans receivable. This is the Corporation's responsibility. Its current methodology for estimating an appropriate allowance for losses on loans is inadequate, in our view. The Corporation does not quantify the allowance for sovereign risk by country, for financial statement purposes, based on an assessment of the ability and willingness of the country to repay its debt. In addition, the methodology does not result in a documented link to existing economic and political analyses of sovereign risk. In our opinion, prompt remedial action is needed to implement an adequate methodology for recognizing sovereign risk and to arrive at an appropriate allowance for losses on sovereign loans.

4.18 If an appropriate allowance had been established, the provision for losses on loans would have been significantly increased; net income reported by the Corporation would have become a significant loss for the year; and retained earnings would likely have become a deficit.

4.19 The Board of Directors and management are in fundamental disagreement with the Auditor General's opinion. In particular, EDC disagrees with the view that, in the case of some of its loans, the principal may not be ultimately collectible in full. EDC has pointed out that the Government of Canada, as stated in its accounting policies in the Public Accounts, shares EDC's views on accounting for sovereign loans. However, the Auditor General disagrees with the Government of Canada's accounting policy. The Auditor General has also qualified his opinion on the Public Accounts of Canada with respect to inadequate recognition of sovereign risk.

Farm Credit Corporation - Decision to Delay Special Examination Beyond Statutory Deadline

> The Farm Credit Corporation (FCC) has decided to defer the completion of a special examination of its systems and practices to a date that is after the deadline established by Part X of the Financial Administration Act.

4.20 Sub-section 138(1) of Part X of the Financial Administration Act (FAA) requires that specified Crown corporations cause a special examination to be carried out. The purpose of the special examination is to determine whether the corporation has maintained systems and practices in a manner that provided reasonable assurance that:

- the assets of the corporation were safeguarded and controlled;
- the resources of the corporation were managed economically and efficiently; and
- the operations of the corporation were carried out effectively.

4.21 The FAA also requires that a special examination of each specified corporation be carried out at least once every five years. The deadline for completion of the first round of special examinations is 1 September 1989.

4.22 The Farm Credit Corporation has recently undergone a period of considerable change, partly in response to the substantial losses it has incurred in recent years. In the year ended 31 March 1988, the Corporation incurred a loss of $512 million, bringing its accumulated deficit to $855 million. At 31 March 1989, the accumulated deficit had increased to $890 million. In the summer of 1988, Cabinet approved a recovery plan for the Corporation. In response, FCC initiated a number of significant changes to its systems and practices. It then concluded that these changes brought into question the value to its Board of a special examination of its prior methods but that an early review of its new systems would be very valuable.

4.23 Accordingly, FCC's Board decided on 15 December 1988 that December 1990 be established as a target date for completion of the special examination. While this was a justifiable decision from management's point of view, it is not in accordance with Part X of the FAA which requires that the special examination be completed by 1 September 1989.

4.24 The audit report issued by the Auditor General in connection with the Farm Credit Corporation's financial statements as at and for the year ended 31 March 1989 has been qualified to reflect the Board's decision to defer the completion of the special examination which is contrary to Part X of the FAA.

International Centre for Human Rights and Democratic Development - Inability of the Centre to Prepare and Provide Financial Statements for Audit

> Because no one has been appointed to represent the International Centre for Human Rights and Democratic Development, no annual report or financial statements have been prepared for the year ended 31 March 1989 as required by the Centre's incorporating Act. We have, therefore, been unable to conduct an audit, as required under Section 31 of the Act.

4.25 In September 1988, the International Centre for Human Rights and Democratic Development was established as a corporation by an Act of Parliament. Section 31 of the Act requires that, within four months after the end of each fiscal year, the Chairman of the Corporation transmit to the Minister (External Affairs) a report on the activities of the Centre for that fiscal year, including its financial statements and the Auditor General's audit opinion thereon.

4.26 As section 28 of the Act requires that the Centre be paid $1 million out of the Consolidated Revenue Fund in the fiscal year ended 31 March 1989, the Canadian International Development Agency (CIDA) issued a cheque dated 26 March 1989 for this amount, payable to the Centre. No one representing the Centre was available to receive the funds.

4.27 As of 31 July 1989, no chairman, director or employee of the Centre had been appointed or hired. As a result, not only did the cheque remain unclaimed from CIDA, but also no annual report or financial statements have been prepared as required by the Act.

4.28 We have, therefore, been unable to audit the Centre's financial accounts and transactions as required by section 31 of the Act.

Observations on Departmental Operations

Atlantic Canada Opportunities Agency - Failure to Include Restrictive Performance Clauses in a Contribution Agreement as Contemplated in Ministerial Approval

> When it entered into a repayable contribution agreement to assist a company's research and development program, the Atlantic Canada Opportunities Agency (ACOA) failed to include restrictive performance clauses requiring the company to carry out at least $12 million of the program in a new facility in Sydney, Cape Breton. Ministerial approval for the assistance was given on the understanding that these clauses would be included. The absence of restrictive performance clauses allowed the company to carry out the research and development program at its other facilities outside Atlantic Canada.

4.29 The Atlantic Canada Opportunities Agency's objective is "to support and promote opportunity for economic development of Atlantic Canada ...".

4.30 In 1988 ACOA entered into a repayable contribution agreement, under the ACOA Action Program, to assist a recipient in carrying out a research and development program costing $24 million. Ministerial authority was given for the agreement on the understanding that $12 million of the program costs would be incurred at a new facility in Sydney, Cape Breton. The ACOA contribution was to be 60 percent of actual eligible costs to a maximum of $9 million.

4.31 The performance clauses in the signed agreement did not include a reference to the $12 million allocation for the Sydney facility and required the recipient to make only "best efforts" to purchase from Atlantic Canada suppliers.

4.32 The failure to include these restrictive performance clauses permitted the recipient to direct the research and development activities to its other facilities outside Atlantic Canada.

4.33 Senior management has informed our Office of its intention to renegotiate the agreement, to better reflect the performance clauses contemplated in the ministerial approval.

Department of Agriculture - Contribution Payment in Advance of Need

> A $1.2 million contribution payment was made to the Province of Quebec in March 1988. In our opinion, $600,000 of this amount was paid in advance of need, resulting in additional financing costs to the government of some $50,000. This represents poor cash management and is inconsistent with Treasury Board guidelines on contribution payments.

4.34 Order in Council P.C. 1986-1 2747 provided authority (pursuant to section 5 of the Department of Agriculture Act) to the Minister of Agriculture to enter into the Canada-Quebec Agri-Food Development Subsidiary Agreement for 1987-90. Under the Agreement, Canada and the Province of Quebec agreed to share equally the costs of programs and projects set out in the Agreement up to a maximum contribution by each government of $17.5 million.

4.35 One of the projects was a $3 million inventory of soil degradation problems for which the Province of Quebec submitted partial costs of $1.2 million in March 1988. The Department, judging that the project would ultimately be completed and the $1.2 million eventually payable, reimbursed the Province for the full $1.2 million. This represented a payment in advance of need of $600.000 -- funds which the government did not yet owe and which would otherwise have lapsed.

4.36 According to Treasury Board guidelines on grants, contributions and other transfer payments, "... a contribution paid in advance of need effectively costs the government more than the face value of the payment since interest and financial costs need to be taken into account".

4.37 Based on the estimated dates that the payments might otherwise have been due, and calculating interest at the 90-day Treasury Bill rate, the government's financing cost on the $600,000 paid in advance of need was approximately $50,000.

Department of Agriculture - Erosion of Accountability and of Parliamentary Control

> The Department of Agriculture has made extensive use of section 5 of the Department of Agriculture Act and Governor in Council authority to create new programs. The Act conveys broad powers to the Minister and Governor in Council, which the Department has used frequently to set up new programs involving billions of dollars. Information presented to Parliament on the objectives and impacts of these programs is inadequate. In at least one case (a program involving $1 billion), a departmental evaluation indicated that the program may have been ill-conceived. Had legislation been introduced to establish the program, with an opportunity for Parliament to consider and debate its purpose, a better-designed program might have resulted.

4.38 Section 5 of the Department of Agriculture Act provides that the "Governor in Council may assign any other power or duty to the Minister". The Department has used this provision in recent years to create or amend dozens of programs that have no other basis in legislation. For example, in the year ended 31 March 1989, at least 22 Orders in Council were passed pursuant, in whole or in part, to section 5 of the Act. These Orders in Council authorized or amended 12 programs involving some $120 million. (In 1987-88, at least 19 Orders in Council dealt with 8 programs representing $153 million.) Payments made under individual programs range from a few thousand dollars to many millions of dollars.

4.39 Another major government department had a similar provision in its Act until 1927 when it was removed by Parliament on the basis that it was unnecessary in view of provisions in the Public Service Rearrangement and Transfer of Duties Act (PSRTDA). These provisions authorize the Governor in Council to transfer powers, duties or functions of any part of the public service from one minister or department to another. The PSRTDA does not say, however, that the Governor in Council has the authority to create powers or programs. In our opinion, this is a prerogative of Parliament which is being eroded when section 5 of the Department of Agriculture Act is used to create major programs.

4.40 In using section 5 of the Act in this way, although the Department notes that it has complied with all government requirements for proper disclosure, the result is that Parliament is provided with little specific information on significant departmental programs. Parliament has little opportunity to debate them, and little basis for monitoring and controlling them, even though it is being asked to vote moneys to fund them.

4.41 In our 1987 Report, we questioned the Department's use of section 5 to create the $1 billion 1986 Special Canadian Grains Program. The 1986 Program was followed by the 1987 Special Canadian Grains Program, involving $1.1 billion, and the Crop Drought Assistance Program at $850 million. These three programs, totalling almost $3 billion, and other programs authorized in this way, are not adequately supported by legislation that establishes their objectives, policy and administrative frameworks, terms and conditions and eligibility criteria. Most importantly, they were established without Parliament having had the opportunity to fully debate them. We should note that approval of the necessary funding through the Estimates process was sought by the Department. However, in our view, hearings on the Estimates are designed to give approval to spend money for purposes and programs that have already been properly debated in the legislative process. Accordingly, they do not provide for the extensive and searching scrutiny of programs that the legislative process does. Indeed, the Speaker of the House of Commons, on 22 March 1977, noted as follows:

> ...it is my view that the government receives from Parliament the authority to act through the passage of legislation and receives the money to finance such authorized action through the passage by Parliament of an appropriation act. A supply item in my opinion ought not, therefore, to be used to obtain authority which is the proper subject of legislation.

4.42 A departmental study, entitled "The Interface Between Stabilization and Special Assistance Programs in the Canadian Grain Sector", of the 1986 Special Canadian Grains Program (SCGP) indicated that there were significant flaws in the way the program had been designed and implemented. For example, the study points out that the program provided for payments based on the "degree of injury". However, it goes on to point out that, "This degree of injury is less after stabilization payments have been factored in, but [in the case of this program] was measured prior to such stabilization. Once WGSA and ASA [Western Grain Stabilization Act and Agricultural Stabilization Act] payments have been received, the degree of injury may not have been below the safety net level". Indeed, the program may not have been needed at all. In response to the question, "Was a 1986-87 SCGP needed?" the study responds, "In 1986, stabilized prices were close to or over the safety net, if this is defined as 120 percent of cash costs. Compensation in this case may not have been needed for the 1986 crop" Had Parliament had the opportunity to fully debate this extensive program, some of these points might have been brought out before the program was implemented.

4.43 We are also concerned about the use of section 5 to provide assistance of up to $5.3 million to producers of red delicious apples. The terms of the Agricultural Stabilization Act (ASA) preclude stabilization payments beyond those provided by a tripartite stabilization plan authorized by the Governor in Council on 18 June 1987. Nevertheless, the Department made additional payments to these producers by creating a program pursuant to section 5. In effect, in this instance, the Department has used the broad authority given in section 5 of the Act to do something disallowed by more specific and more recent legislation.

4.44 With respect to the assistance payments to red delicious apple producers, the Department replies that, while it agrees with our interpretation of the ASA, the ASA does not preclude any other assistance which could be afforded under other legislation. However, in its discussion of the reasons for the payment, it is clear that the intent of the payment was price stabilization, based on the view that the tripartite level of stabilization was not adequate in these particular circumstances. The use of section 5 of the Department of Agriculture Act to make these payments, whether technically legal or not, circumvents Parliament's requirement, as expressed in the ASA, that there be no further price stabilization payments if a tripartite agreement is in place for the commodity.

4.45 The Department has also pointed out that its legal advisers have indicated that, in their opinion, section 5 of the Department of Agriculture Act provides an adequate legal basis for the actions described. However, we must note that our primary concern is not with the narrow legality of the Department's use of this provision but rather with its impact on Parliament's ability to carry out its role.

4.46 There have not been any significant amendments to the Department of Agriculture Act for many years. In our view, the government's extensive and varied use of section 5 of the Act presents a threat to Parliament's role. Parliament should be given the opportunity to review the Act and decide whether section 5 should continue to be used in this manner.

Department of Agriculture - Tripartite Program for Sugar Beets is not Meeting the Legal Requirement to be Financially Self-sustaining

> In our opinion, the National Tripartite Price Stabilization Program for sugar beets is not financially self-sustaining, although it is required to be by the Agricultural Stabilization Act. Furthermore, there are serious deficiencies in the Department's analyses of the program's viability. Information presented to the Minister of Finance when advances were requested to meet funding shortfalls was inadequate.

The Tripartite Stabilization Programs

4.47 The Department of Agriculture has established Tripartite Stabilization Programs for various agricultural commodities to stabilize the receipts of participating producers. This is in part accomplished through stabilization payments made to producers when the average market price of the commodity falls below a calculated support price. The programs are established and operate under the authority of the Agricultural Stabilization Act, Governor in Council approvals and agreements between Canada and participating provinces. Funding of the programs is shared equally by Canada, participating provinces and participating producers subject to maximum contribution levels by Canada and the provinces. A Stabilization Committee, made up of federal, provincial and producer representatives, has been established for each program.

4.48 The Act requires that the level of premiums paid by producers must be such as will, along with government contributions and interest received, make each program financially "self-sustaining". The agreements have defined this to mean that, over time, premiums, government contributions and interest received should equal stabilization payments and interest paid.

Financial Situation of Sugar Beet Program

4.49 In our opinion, the sugar beet program is not financially viable under the existing arrangements nor is it likely to be so, given current forecasts. In its first year of operation, covering the 1987 crop, revenues (producer premiums plus federal and provincial contributions) totalled $2.5 million but stabilization payments amounted to $14.5 million, resulting in a deficit of $12 million, averaging over $12,000 for each participating producer. Based on preliminary departmental forecasts, after the 1988 crop, the accumulated deficit, including interest charges on the previous deficit, will be approximately $17 million.

Minister of Finance's Concerns

4.50 In authorizing advances to the sugar beet tripartite program to cover funding deficiencies, the Minister of Finance also expressed concerns, on two separate occasions, about the viability of the program. In approving the second advance, he noted that "until the actuarial soundness of the sugar beet plan is confirmed..., it would be extremely difficult for me to justify the provision of any future advances to this program".

Departmental Analysis of Financial Viability

4.51 We share the Minister of Finance's concerns and are also concerned about what we believe to be serious deficiencies in the Department's earlier analyses of the program's viability. Such analyses are fraught with all the difficulties of trying to predict the future. This is even more difficult in the context of the extremely volatile market for sugar beets in the past decade. For example, Canadian prices for sugar have ranged from $80 per tonne in 1979 to $25 per tonne in 1986. In our view, this emphasizes the need for conservatism in assumptions and predictions and for sensitivity analysis of the various assumptions, including an analysis of worst- and best-case scenarios.

4.52 We have reviewed earlier departmental analyses which concluded that the tripartite program for sugar beets had the potential to be viable by 1996. These were based on very optimistic assumptions and did not adequately consider the unique nature of the various market forces affecting sugar beet prices. For example, these analyses generally assumed that historical price patterns would repeat in the next decade and, therefore, projected prices of over $70 per tonne for 1989 and about $60 per tonne for 1990. In early 1989, world prices ranged from $30 to $40 per tonne. Another of the many assumptions is that costs of production will be affected by one percent inflation per year. The Department's own data indicate that, in recent years, costs of production for sugar beets have risen by an average of 7.2 percent each year. More recent departmental analyses undertaken in the spring and summer of 1989 have used more varied and realistic assumptions and have arrived at less optimistic conclusions.

Stabilization Payment Rate for 1987 Sugar Beets

4.53 We are also concerned about the unusual way the stabilization payment rate was calculated for the 1987 sugar beet crop -- one of the major causes, in our view, of the program's current financial difficulties. The agreement requires that the calculation be based on the "current cash costs of production". Calculating the costs of production involves converting costs per acre to costs per standard tonne. For 1987, the Department based its calculation on costs per acre for 1987 and average yield from 1982 to 1986 -- a cost of production based on costs in one year and yields in others. This resulted in stabilization payments based on production costs of $660 per acre, when in fact the current cost per acre has been estimated at $470. Had the 1987 yield been used, stabilization payments totalling $14.5 million would have been reduced to $6.6 million.

4.54 In the view of departmental officials, the use of a five-year average yield is an integral part of the cost-of-production model which the Stabilization Committee has the authority to establish and amend. In our view, however, the agreement requires that the model use current costs of production, which must be determined on the basis of current yields if the results are to be meaningful.

Conclusions

4.55 Based on our review of the Department's viability analyses and our own analyses, we have concluded that the sugar beet program is not self-sustaining. Information presented to the Minister of Finance when advances to the program were sought was inadequate. In our view, the Department's analyses of the program's viability were deficient in a number of important respects and the Department had not adequately considered how to restore the viability of the program.

4.56 We have reviewed the Department's analyses of financial viability for only the sugar beet tripartite program. In light of the size and number of tripartite and other stabilization programs, we are considering undertaking a more comprehensive review of the Department's stabilization programs in future years.

Department of the Environment - Lack of Expenditure Authority

> The Canadian Parks Service (CPS) does not have the authority under the Historic Sites and Monuments Act to spend funds for the display and administration of the St. Roch Historic Site in Vancouver. In recent years, CPS has spent in excess of $200,000 annually on this site. The St. Roch, a former Royal Canadian Mounted Policy supply vessel, is known for its 1942 voyage through the Northwest Passage. It is now owned by the City of Vancouver and is designated a National Historic Site by CPS.

4.57 In 1965 an agreement was signed between CPS and the City of Vancouver which stipulated that CPS would restore and furnish the vessel and the City would assume responsibility for its display, care, supervision and protection.

4.58 The Canadian Parks Service has stated that in 1974, the year the site was opened to the public, the City indicated that it could not afford to display the vessel. The Canadian Parks Service assumed this responsibility, and has continued its financial and operational support ever since. Under the Historic Sites and Monuments Act, CPS may only spend money on sites which it owns or for which it has received Governor in Council authority. In effect, CPS has accepted responsibility for all maintenance associated with the vessel and its shelter, acquisition and maintenance of the vessel's furnishings, janitorial services, monitoring and repair of the fire and intrusion systems, guide services, a share of the educational literature associated with the vessel and all visitor services and surveillance within the vessel shelter. The City maintains the grounds and parking lot, provides light and heat for the shelter, and provides office and work space for staff and washroom facilities for staff and the public.

4.59 The Canadian Parks Service continues to pursue alternatives for the display of this historic site that could lead to the resolution of the authority issue.

Department of External Affairs - Insufficient Disclosure to Parliament of Planned Expenditures on Export Trade

> The government's expenditures on international trade are made in a number of ways. One way is through the "Canada Account" included in the books and records of the Department of External Affairs and administered by the Export Development Corporation (EDC). In our view, Parliament is not given enough information to understand the nature, purpose and magnitude of planned expenditures on export trade relating to the Canada Account. Plans submitted to Parliament by the Department of External Affairs and EDC do not contain explanations of costs and intended benefits of these trade related expenditures, and we could not determine which government organization is accountable for justifying decisions or for their results.

4.60 Part II of the Estimates for the Department of External Affairs indicates that the planned levels of disbursements through the Canada Account are $176 million for 1988-89 and $225 million for 1989-90. This represents a significant portion of government expenditures on international trade development.

4.61 The Export Development Act provides for loans, insurance and guarantees for the purpose of facilitating and developing export trade. Contracts which, in the opinion of EDC's Board of Directors, involve risks for a term or an amount in excess of that "normally" undertaken by the Corporation, may be entered into under the authority of the Governor in Council when the Minister for International Trade considers them to be in the national interest. These contracts are funded through External Affairs appropriations out of the Consolidated Revenue Fund and the related transactions are referred to as the Canada Account.

4.62 The contracts are often entered into at highly concessional terms, such as low interest rates and long periods of repayment. EDC and External Affairs officials informed us that concessional terms are established by international understanding. In some cases, countries which have received such loans have subsequently experienced some repayment difficulties. For example, a loan of $17.6 million was made in 1987-88 to an African country, at no interest for a 50-year repayment term. Loans of over $100 million to an East European country remain outstanding, without significant repayment for many years. There is an annual cost to Canadians resulting from the concessional loan terms, the losses likely to be incurred if loans are not fully repaid, and the continuing cost of administering these contracts.

4.63 Although the Minister for International Trade is ultimately accountable to Parliament, no reference to these moneys has been made by the Department in Part III of the Estimates. Thus, the Canada Account has not been considered a departmental program activity for which the Department is accountable. EDC, on the other hand, has stated that its accountability for the Canada Account is limited to ensuring that it is administered in a sound manner, and that the Corporation has not been required to provide justification for the moneys spent or to report on the overall net economic benefits to Canada arising from its activities. The Office of the Comptroller General acknowledges the need for appropriate disclosure to Parliament of all planned expenditures on export trade, and for reporting on their results, but has not provided specific recommendations or guidelines to either the Department of External Affairs or EDC.

4.64 We have been unable to determine which arm of the government is accountable for providing information to Parliament justifying moneys spent and stating the costs and benefits to Canadians of facilitating and developing export trade through the operations of the Canada Account.

4.65 Given the need for accountability to Parliament for the substantial public moneys relating to the Canada Account, its operations should be disclosed either as an activity of the Department of External Affairs -- and therefore included in its Part IIIs -- or as an activity of EDC in its Summary Corporate Plan, or by some other appropriate means to be determined by the government.

4.66 Officials of the Department of External Affairs have informed us that the Department and EDC believe that it would be useful to provide additional information to Parliament to enable it to understand this important program and that they and EDC will work together to achieve this objective.

Department of Finance - Duplicate Accounting Records for Public Debt

> Accounting records for domestic public debt are maintained by both the Department of Finance and the Bank of Canada. We estimate that annual savings of about $100,000 could result from eliminating this duplication of records.

4.67 The Bank of Canada is the fiscal agent and registrar for the Government of Canada's domestic public debt, including Canada Marketable Bonds, Canada Savings Bonds and Treasury Bills. The Bank maintains records of the issuance and retirement of these securities, and the interest paid on them. In 1988-89, these transactions amounted to $545 billion.

4.68 The Department of Finance also maintains accounting records for these securities based on information provided by the Bank of Canada. The Department uses these records to calculate and record accrued interest for public accounts purposes. At year end, the accounting records of the Department and the Bank are reconciled.

4.69 In our opinion, there is no need to maintain duplicate accounting records. We estimate that eliminating this duplication could result in annual savings of $100,000 Accordingly, we believe that this situation should be reviewed.

4.70 Officials of the Department of Finance are currently reviewing this matter with officials of the Bank of Canada.

Department of Finance - Failure to Plug a Loophole in the Excise Tax Act Results in Increased Federal Sales Tax Rates and could have a Negative Effect on the Equity and Integrity of the Tax System

> A key anti-avoidance rule in the Excise Tax Act is ineffective. The failure of the Department of Finance to correct the problem is causing annual revenue losses of at least $300 million that are being offset by increased federal sales tax rates.

4.71 A basic principle of Canadian tax law is that a taxpayer is entitled to arrange his or her affairs to attract the minimum amount of tax. This right is subject, however, to specific and general statutory anti-avoidance rules. Section 58 (formerly section 34) of the Excise Tax Act is an anti-avoidance rule It is intended to discourage taxpayers from entering into non-arm's length transactions solely to gain a tax advantage.

4.72 The base for the federal sales tax is the selling price charged by the manufacturer. If the manufacturer is also responsible for research and development expenses, transportation costs, warranties, advertising and other marketing and distribution costs, then the selling price will include such costs. If, on the other hand, the manufacturer sells the goods to an agent or affiliated company that bears the responsibility for these associated costs, the manufacturer's selling price, which is the base for tax purposes, will be significantly lower.

4.73 Some manufacturers created marketing companies through which to sell their goods in order to gain a tax advantage. By using section 58 and setting the fair sale price of goods at the value for which the goods were sold to an arm's-length purchaser, the Minister of National Revenue was often successful in negating this tax advantage. However, the section is unable to upset a well-structured transaction.

4.74 A 1986 Federal Court of Canada decision confirmed that section 58 is ineffective in preventing manufacturers from avoiding tax by establishing related marketing companies.

4.75 Taxpayers are thus able to avoid tax in a way that was not intended. Although amendments to section 58 were made in 1988 to ensure that taxpayers are not able to set artificially low transfer prices to related marketing companies, the government still estimates that the avoidance mechanism is costing the treasury between $300 million and $350 million annually in lost revenue. In order to protect revenues, further legislative amendments are required.

4.76 In the June 1987 White Paper on Tax Reform, the government presented a proposal to deal with the problem. The proposal proved unworkable and was withdrawn in the February 1988 Budget. At that time the government presented a second proposal to proceed, effective 1 November 1988, with amendments to the Excise Tax Act. This proposal involved a complex method of adjusting all manufacturers' selling prices to take into account marketing and distribution costs in order to relieve the problem of tax avoidance and to correct the biases inherent in the Excise Tax Act.

4.77 Ultimately, in the April 1989 Budget the government announced that it would not close the loophole. The government stated that the problem would be eliminated with the introduction of the proposed new Goods and Services Tax on 1 January 1991 and that therefore it would not be reasonable to introduce the proposed changes, given the additional compliance and administrative burden they would entail and the short period before the introduction of the new tax. In the interim, the estimated $300 million to $350 million in lost annual revenue would be offset by increasing federal sales tax rates. Increased tax rates magnify the biases inherent in the Excise Tax Act; they also provide an additional benefit to taxpayers using the marketing company avoidance mechanism.

4.78 We are concerned that the government failed to correct an identified tax avoidance problem. The proliferation of marketing companies will cost the treasury at least $300 million a year until at least 1 January 1991. The ability to rectify problems through timely legislative action is critical to the administration of a commodity tax system because retroactive legislation can impose serious hardships.

4.79 We are also concerned because tax avoidance schemes have a negative effect on the equity and integrity of the tax system and on attitudes to voluntary compliance. Access to such schemes is usually restricted to those who can afford expensive start-up and running costs.

Department of Finance - Non-compliance with the Financial Administration Act

> During 1988-89, the Department of Finance failed to obtain Governor in Council approval, as required by the Financial Administration Act, for the issue of $2 billion in Treasury Bills.

4.80 Borrowing authority Acts provide Parliamentary authority for the net amount of new debt issues, less redemptions, during a fiscal year. The Financial Administration Act provides additional controls over the financing of the debt. Under sections 44 and 46 of the Act, Governor in Council approval is required for the issue of the various types of financial securities.

4.81 While the overall new borrowings authorized for 1988-89 were not exceeded, the Department of Finance failed to obtain the required Governor in Council approval for the issue of $2 billion in Treasury Bills during the first quarter of 1988-89.

4.82 Officials of the Department of Finance informed us that this situation stemmed from an unexpectedly large rollover of Treasury Bills during the first quarter of the year. New procedures have since been implemented to prevent further recurrence.

Department of Regional Industrial Expansion - Serious Deficiencies in the Approval Process and Administration of Two Contributions Totalling $27.7 Million

> In June 1988, the Department of Regional Industrial Expansion (DRIE) made a payment of $238,000 to a defence electronics company. This was the final payment of a $13.3 million repayable contribution for an avionics displays project funded under the Defence Industry Productivity Program (DIPP). In May 1989, $6.3 million was paid to the same company as part of another repayable contribution of $14.4 million for a related project funded under DIPP. We observed a number of serious deficiencies in the approval process for these projects. Subsequent project administration and monitoring were also inadequate.

4.83 A $6.2 million repayable contribution for phases A and B of a project was originally approved by the DRIE Minister on 12 February 1986. An amendment to the project, approved by the Minister on 19 March 1987, increased the contribution by $7.1 million, bringing the total to $13.3 million. This was beyond the $10 million authority delegated to DRIE, making Treasury Board approval a requirement. This approval was not obtained. Documentation submitted to the Minister for approval of the $7.1 million amendment did not indicate that it would bring total DIPP funding to over $10 million.

4.84 On 9 March 1989, DRIE obtained Treasury Board approval for a $14.4 million repayable contribution to the same company for a related project. There was a considerable amount of information contained in the project documentation to indicate that it was a continuation of the previous project. This contribution increased the total DIPP funding to $27.7 million. Although funding in excess of $20 million to one company for continuation of a project requires Cabinet approval, it was not sought because this contribution was treated by DRIE as a separate project.

4.85 To be eligible for assistance, a project must need DIPP support in order to proceed. DRIE documentation on the initial project in January 1986 indicated that the project had been under way since April 1984 because the company did not want to miss business opportunities. The project analysis did not explain how the project could be considered eligible in these circumstances. A project audit, carried out by the Audit Services Bureau (ASB) of the Department of Supply and Services (DSS), indicated that the company had begun work on the project as early as February 1983 and that some sales had occurred prior to July 1985.

4.86 The project summary dated August 1988 for the second contribution of $14.4 million indicated that this project would go ahead without DIPP funding, although the company might then miss anticipated market opportunities and have to drop other lesser projects.

Other documentation indicated that work on this project had started in August 1987 in order to take advantage of these markets.

4.87 For both projects, DRIE allowed the company to claim retroactive reimbursement for costs incurred. This did not appear to be consistent with the directive governing retroactivity in the administration of DIPP which permits retroactivity to the date DRIE receives full disclosure of information on a project.

- The first project was approved 12 February 1986, although the final proposal was received by DRIE in March 1986. This proposal referred to an original submission in March 1985. Costs were allowed retroactive to 1 April 1984.

- In the second project, DRIE had received a draft proposal dated 20 January 1988. The application and final proposal for funding were received on 8 April 1988. This project was approved on 9 March 1989. Retroactivity was allowed to 1 March 1988 -- the day after the company had reached the maximum costs allowed under the first project.

4.88 Under the contribution agreement, proceeds from sales are to be deducted from eligible costs. The agreement also states that the company's records of costs and sales are to be open to audit. In an audit report to DRIE in November 1987, ASB indicated that sales had taken place before July 1985 and that the company had denied the auditors access to sales records. It was therefore impossible to determine the total possible overpayment by DRIE. No action was taken by DRIE even though this denial of access meant that the company was in default of its contract. ASB repeated its audit qualification in May 1989.

4.89 The company was also required to report sales resulting from work funded under the agreement. No indication was found on file that the company had informed DRIE of sales that occurred prior to July 1985. There were other indications on file of sales from August 1985 to July 1987 but DRIE had not followed these up to determine why the company had reported a zero dollar sales figure for this period.

4.90 We also observed that some key information provided during the decision-making process for the $14.4 million repayable contribution was inaccurate and incomplete.

- The project proposal sent to the Minister requested DIPP funding for 50 percent of project costs. The documentation referred to two previous projects for which DIPP contributions had represented 50 percent of project costs. In fact, the level of DIPP funding for these projects had been less. The $6.2 million contribution represented 35 percent of project costs and the amendment for $7.1 million represented 42.5 percent of costs. A contribution for a $2.9 million capital project had also been funded at 35 percent of costs.

- Potential sales referred to in the proposal to the Minister and in the Treasury Board submission were considerably higher than the projections in the company's final proposal.

- In the Treasury Board submission, DRIE indicated that the company had never paid out any dividends. This was not the case. A $4.2 million dividend was paid in 1987 from 1986 profits.

4.91 The $14.4 million contribution was to be fully repayable, based on a percentage of sales of all display products. The wording of the contract entered into for this contribution called for repayment to begin after the initial $6.2 million project and $7.1 million amendment had been fully repaid. However, we observed that the contract for the first project called for repayment to begin only after $25 million in annual sales of products specifically included in the contract had been reached. The wording of these repayment clauses could result in non-repayment of the contributions, particularly if sales from the first contract are lower than expected.

4.92 The first contribution, totalling $13.3 million, has been fully paid to the company. Any DRIE overpayment will have to be recovered. An overpayment of $314,000 has been identified by ASB. Repayment has been requested by DSS.

4.93 DRIE has reviewed our observations and re-examined these projects. Documentation has been prepared which describes the technical specifications to be met by the product under the second project and those the company had achieved by March 1988. DRIE is satisfied that, although the two projects are closely linked, these specifications are different enough that the projects were separate. In terms of the need for DIPP support, DRIE has indicated that the $14.4 million contribution was essential if the company was to meet the minimum technological requirements on time to take advantage of major market opportunities. Although DRIE has indicated that, in its opinion, the projects were separate and eligible for DIPP funding, it has acknowledged that the documentation and analysis supporting these projects were inconsistent and lacking in a number of areas.

4.94 With respect to retroactivity, DRIE has also indicated that it believes the retroactive costs in both projects were appropriately allowed although these were not adequately supported by information on file.

4.95 The issue of access by ASB to sales information is being addressed, as is the recovery of the overpayment. One repayment of $160,517 has been received and a second is under negotiation. DIRE has also advised us of its intent to seek a contract amendment to clarify the original intent of the parties that all product sales be considered with respect to repayment.

Department of Supply and Services - Difficulties in the Acquisition of Crash Firefighting and Rescue Vehicles

In 1986, the Department of Supply and Services (DSS) entered into procurement contracts to provide the Department of Transport (DOT) with crash firefighting and rescue vehicles for use at airports operated by DOT. The contracts were for 68 Rapid Intervention Vehicles (RIVs) costing $22.1 million.

According to information in DSS and DOT files, this acquisition encountered significant difficulties. The consequences included:

- additional costs of approximately $1 million arising from the initial splitting of the contract requirement between two suppliers and the subsequent reversal of this arrangement;
- a government payment of $290,000 to terminate a contract with one of the suppliers; and
- a time span of over four years to complete a procurement of equipment that was urgently needed for public safety.

4.96 We noted considerable delays in awarding the RIV contract. Although DOT's request for the vehicles was made in the period January to July 1984, the first contract -- for 34 vehicles -- was not awarded by the government to Supplier A until April 1986. A second contract -- for the remaining 34 vehicles -- was not awarded to Supplier B until September 1986.

4.97 The contract requirement was split and awarded to two suppliers despite DSS and DOT concerns in 1986 that Supplier B might not have had the necessary capabilities to perform the work. As well, DOT officials had expressed their preference for awarding the entire project to Supplier A, who it was believed had the appropriate expertise. We were advised by Supplier B that it had the full capability to complete the work.

4.98 By splitting the requirement, the government sought to achieve other objectives, namely, to reduce the risk of late deliveries -- because of the urgency of the need for the vehicles -- to create a second source of supply, to encourage technological development, and to create additional employment opportunities. As a result of splitting the contract requirement, the total contracted price for all the required vehicles amounted to $22.1 million instead of $20.2 million, the amount initially bid by Supplier A.

4.99 Eight months after signing, Supplier B advised the government that it could not perform in accordance with the contract and requested that the contract be terminated by mutual consent. Subsequently, Supplier B advised us that it had to terminate this contract due to difficulties in dealing with government officials at that time.

4.100 Under the Termination for Default provisions of the contract, the government could have terminated it 45 days after giving notice to the supplier of its default. Instead of applying this provision, the government paid Supplier B $290,000 and released it from the contract. DSS indicated that this payment was made to enable the supplier to maintain its financial viability. In addition, DSS stated that this payment would allow it to accept a time-limited offer from Supplier A for the production of all units originally assigned to Supplier B.

4.101 Finally, in May 1987, Supplier A's initial contract for 34 vehicles was extended to include the entire requirement for 68 vehicles at a cost of $21.3 million, approximately $1 million higher than its original bid of $20.2 million for the 68 vehicles.

4.102 In 1983, DOT had indicated, in its funding request for this procurement, that its current standards of crash firefighting and rescue services dated back to 1962 and related to aircraft of a bygone era. DOT had determined that there was an urgent need to replace its existing vehicles which did not meet the revised standards of the International Civil Aviation Organization. This urgency was expressed to DSS at various points in the procurement process.

4.103 Despite this urgency, more than four years elapsed between DOT's requisition for the vehicles and the date the deliveries were completed in 1988. DSS advised us that, in its opinion, the technical sophistication of the vehicles prevented an earlier completion of the procurement.

4.104 Nevertheless, we are concerned that the protraction of this project could have had an impact on public safety. We believe that any urgent procurement involving significant safety equipment should be completed more expeditiously.

Department of Supply and Services and Department of Fisheries and Oceans - Unacceptable Contracting Practices

> Unacceptable contracting practices in the acquisition of computer services resulted in a dispute with the supplier over the adequacy of the fees paid.

4.105 In 1987, the Department of Supply and Services (DSS) contracted for computer processing and support services relating to a financial management system (FMS) for the Department of Fisheries and Oceans (DFO). The contract, as amended in 1988, provided for the services at a fixed monthly fee of $50,000, for five months with an option to extend the contract for any period up to three months beyond the expiration date.

4.106 Before the contract ended, DSS became aware that a continuation of services would be needed after the expiration date. In response to a request from DFO, DSS asked the supplier to extend the contract for an additional month under the same terms and conditions. However, neither DSS nor DFO gave the notice within the time required to take up the contract option and accordingly, the contract expired.

4.107 Notwithstanding the expiration, the supplier continued to provide service even though it had expressed concern over the increased workload and costs for the project. A dispute then arose and the supplier claimed compensation of $671,000 for the one month extension requested by the departments, and submitted another claim for $615,000 to cover an apparent increase in the workload during the initial five months of the contract.

4.108 We were advised by DSS and DFO that the workload was indeed larger than had been envisaged by the contract. DSS and DFO negotiated a final settlement of the dispute, and of all claims, with the supplier for $250,000 and amended the contract accordingly. However, this amendment, made in the new fiscal year, stated that the payment of $250,000 was for additional services provided during the month of June 1988 -- within the optional extension period provided for in the original contract. DSS informed us that DFO was unable to amend its contract requisition to take advantage of the option. DFO acknowledged that the additional services had thus been rendered without a bona fide contract in place.

4.109 In our view, the performance of additional work by a supplier without proper contract documentation and the failure to take advantage of a contractual option within the required time limits constitute unacceptable contracting practices, which in this case resulted in a dispute.

Departments Need to Reconcile their Financial Records with the General Ledger of Canada on a More Timely Basis

> A significant number of departments have been unable to reconcile their financial records with the General Ledger of Canada on a timely basis. Without timely reconciliations, the reliability of financial information may be questionable and there is an increased risk of errors or omissions.

4.110 Reconciliation is a fundamental accounting control that helps ensure that financial information used by departments for managing agrees with financial information in the General Ledger of Canada used for external reporting. The purpose of reconciling is to detect incomplete or inaccurate information. Reconciliations and other accounting controls are the responsibility of departmental Senior Financial Officers.

4.111 The requirements for timely reconciliations are set out in the Guide on Financial Administration issued by the Office of the Comptroller General and in Receiver General Directives. The Receiver General Directive on Reconciliation was revised as recently as 1987. Most departments have not met the revised reporting requirements. Most failed to reconcile their Payment on Due Date (PODD) liability accounts and more than half of all departments were late filing their monthly reconciliation reports. Some departments were not able to reconcile until well after the year end and in other cases reconciliation reports contained unexplained and uncorrected differences.

4.112 Several of the government's largest departments have recently spent significant amounts of money to install new computer systems to provide management with more sophisticated accounting and internal financial reporting. Reconciling the information in virtually all of these systems with the General Ledger of Canada has proven difficult. In terms of timeliness and quality of reconciliations, the most serious deficiencies arose in these new systems.

4.113 In examining and reporting on the Financial Statements of the Government of Canada (see Section 2, Volume I of the Public Accounts) we were required to perform additional audit procedures because we could not rely on the financial systems to produce complete and accurate information. Although we have not detected material errors affecting Canada's summary statements, there is still a risk that financial information used in the departments concerned may have been inaccurate and thus misleading to those who used it.

4.114 The Office of the Comptroller General is responsible for providing advice and guidance to departments on financial control. Their recent technical publication, Common Evaluation Criteria for Financial Management Systems, intended as a guide for the selection of new financial systems, excludes from the "mandatory" category computerized reconciliation with the General Ledger of Canada. These criteria should be reviewed and amended to ensure that the requirement for reconciliation procedures receives top priority. In addition, departmental Senior Financial Officers should ensure that their financial information systems are agreed monthly with related balances in the General Ledger of Canada, as already required by Receiver General directive.

The matters reported in this chapter are important; but they should not be used to draw conclusions about matters not examined.

4.115 The Office of the Comptroller General and the Receiver General, in conjunction with departments, are undertaking several initiatives to ensure that all departments will in future be able to meet the requirements for timely reconciliations. These initiatives include reviewing the Common Evaluation Criteria, preparing a handbook on reconciliation to be issued by year-end, ensuring new computer systems include reconciliation modules and exploring ways of getting reconciliation data to the departments more quickly.

4.116 Until timely reconciliations are regularly performed, there is no assurance that departmental accounting systems can be relied on for financial and management decision making and external reporting.

5

IMPLEMENTATION OF THE FRAMEWORK FOR THE CONTROL AND ACCOUNTABILITY OF CROWN CORPORATIONS

5

IMPLEMENTATION OF THE FRAMEWORK FOR THE CONTROL AND ACCOUNTABILITY OF CROWN CORPORATIONS

Main Points

5.1 Considerable progress has been made in implementing the framework for the control and accountability of Crown corporations introduced with amendments to the Financial Administration Act in 1984. Some improvements are possible, but most of the important elements are in place (paragraphs 5.87 and 5.88).

5.2 Most informed observers interviewed believe that the framework, as implemented, represents a vast improvement over the previous situation. Our own observations support the view that vigilance and stability have characterized the Crown corporations sector in recent years (5.23 to 5.86).

5.3 The previous framework applied unevenly to a growing population of Crown corporations. One major improvement is that, except for a few that are exempted, the new framework applies to all parent Crown corporations and, through them, to their wholly owned subsidiaries (5.15 to 5.22).

5.4 The legislation and regulations have established a fixed timetable for submitting to government, and for tabling in Parliament as appropriate, the central control and accountability documents. The timetable is closely monitored and generally observed. This is a sign of respect for the framework, and a precondition for its success (5.25 to 5.41).

5.5 The quantity and timeliness of information Parliament receives about Crown corporations has improved significantly. However, its quality is uneven. The most evident weaknesses are in how objectives are articulated and linked to subsequent performance (5.42 to 5.47).

5.6 Explicit roles assigned by the legislation to appropriate ministers and boards of directors, coupled with a "hands-off" stance by central agencies, have encouraged ministers and boards to take their responsibilities seriously. Ministers generally ensure that the accountability and control documents they are asked to endorse are carefully reviewed. Most boards of directors play a meaningful role in managing Crown corporations (5.22 to 5.72).

5.7 The new framework is comprehensive and provides for reasonable balance among the interests of various players. But the framework set out in legislation is not solely responsible for the demonstrated improvements. Strong and sustained attention by all concerned has played an important part in making the system work.

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IMPLEMENTATION OF THE FRAMEWORK FOR THE CONTROL AND ACCOUNTABILITY OF CROWN CORPORATIONS

Introduction

A new control and accountability regime for most Crown corporations

5.8 In June 1984, responding to growing concerns that Crown corporations were not under effective control, Parliament passed Bill C-24, an Act to amend the Financial Administration Act (FAA) in relation to the control of Crown corporations. Bill C-24 established a control and accountability regime for almost all federal Crown corporations by creating a new Part XII of the FAA. Part XII was renumbered to become Part X on 12 December 1988 as a result of the Revised Statutes of Canada, 1985.

5.9 In this chapter we report on the implementation and status of the Part X regime some five years after it came into effect on 1 September 1984. Of necessity, our review focussed on the implementation of the key elements of the control and accountability framework and not on the substantive impact of the regime on the performance and accountability of Crown corporations.

5.10 As defined by the Financial Administration Act, Crown corporations are parent corporations or subsidiaries that are wholly owned, directly or indirectly, by the Crown. Part X provides the framework for the control and accountability of all parent Crown corporations named in Schedule III of the FAA and, through them, of their wholly owned subsidiaries.

5.11 In addition to Crown corporations, the federal government has full or partial ownership interests in a large number of other organizations with a corporate form These include, for example, the "departmental corporations" that carry out administrative, research, supervisory, advisory or regulatory functions of a governmental nature, and corporations that are owned jointly with other governments or private sector interests Because such organizations are not defined as Crown corporations they do not fall within the ambit of the control and accountability framework outlined in Part X.

Background

Developments leading to the introduction of the new regime

5.12 Bill C-24 was introduced in 1984, following a period of mounting concern within Parliament, government and among the public at large about the control, direction and accountability of federal Crown corporations. Until the 1984 amendments to the Financial Administration Act, the control and accountability regime had not changed in any meaningful sense since it was introduced in 1952 (Part VIII of the FAA). During this period, however, there had been significant growth and change in the government's use of the corporate form for implementing public policy.

5.13 The late 1970s and early 1980s saw a growing debate about Crown corporations, fueled in part by specific instances of dubious business practices, huge losses by some Crown corporations, and increased public concern for government accountability. The main focus of the debate was not on the role of Crown corporations as such, but rather on how to strike a proper balance between the need for adequate control and direction by Parliament and government on the one hand, and the need for appropriate independence and accountability of Crown corporations on the other.

5.14 A number of major reviews relating to Crown corporations were completed during this period. These included a "blue paper" published by the Privy Council Office in 1977, the Royal Commission on Financial Management and Accountability (The Lambert Commission), chapters in our 1976, 1979 and 1982 annual reports and a series of reports by the House of Commons Standing Committee on Public Accounts. All of these reviews pointed to the need for a major overhaul of the arrangements then in effect.

Profile of Crown Corporations

New Crown corporations have been promptly scheduled to maintain comprehensive coverage of the regime

5.15 Except for seven parent Crown corporations exempted because of their special natures, all parent Crown corporations were named in Schedule III of the Financial Adminstration Act when it was amended. Furthermore, Part X provides that parent corporations incorporated or acquired after that time have to be named in the schedule within sixty days or be dissolved. Since September 1984, new corporations have been promptly scheduled, and Schedule III remains up to date.

Our review focussed on the implementation of key elements of the Crown corporation control and accountability framework.

5.16 This situation contrasts with that which prevailed before the amended framework was introduced. Then, the legislative framework (Part VIII) applied only to scheduled Crown corporations and not to their wholly owned subsidiaries. In addition, with no requirements for scheduling new corporations, the schedules were not always kept up to date when new corporations were created or acquired, or when corporations changed their status. As a result, the regime was neither comprehensive nor current in its coverage.

5.17 The Financial Administration Act divides parent Crown corporations into two groups:

- Schedule III-Part I includes parent corporations that ordinarily depend on parliamentary appropriations for operating purposes and/or that operate in a non-competitive environment.

- Schedule III-Part II includes parent corporations that, to the satisfaction of the Governor in Council, operate in a competitive environment and do not ordinarily depend on appropriations for operating purposes.

5.18 Exhibit 5.1 shows that at 1 September 1984, there were 46 scheduled parent Crown corporations with 134 wholly owned subsidiaries. Between that date and 31 December 1988, the number of scheduled parent corporations declined to 44, with 125 wholly owned subsidiaries. During the same period, one Crown corporation was added to those that are exempted from the provisions of Part X.

5.19 Exhibit 5.2 emphasizes the importance of keeping the schedules up to date if comprehensive and current coverage of the control and accountability framework is to be maintained. As this exhibit shows, the Crown corporation situation is dynamic. The net change (-2) in the number of scheduled parent corporations is the result of 10 being created and 12 others being either dissolved or privatized during the intervening period.

5.20 Although not shown in Exhibit 5.2, the change (-9) in the number of wholly owned subsidiaries over this period of approximately four years is also the net result of considerable activity in creating or acquiring some, and selling or dissolving others. In the

NUMBER OF CROWN CORPORATIONS

	September 1984	December 1988
Parent Corporations		
Schedule III – Part 1 (1)	37	32
Schedule III – Part 2 (1)	9	12
	46	44
Exempt Corporations	7	8
	53	52
Wholly owned Subsidiaries	134	125
TOTAL	**187**	**177**

(1) Schedule III was Schedule C until 12 December 1988

Exhibit 5.1

year ending 31 March 1988, for example, the number of wholly owned subsidiaries rose from 114 to 125. This increase of 11 resulted from 19 wholly owned subsidiaries being added to the total and 8 being deleted.

5.21 Exhibit 5.3 provides profiles of Crown corporations at 31 July 1985 and 31 July 1988. The table shows that, in 1988, scheduled Crown corporations employed about 135,000 people and had total assets of nearly $49 billion and liabilities of $37 billion. The data show that employment has declined by nearly 20 per cent over the three-year period, while total assets and liabilities have also decreased slightly. Annual budgetary funding from Canada has declined by 23 per cent, from $4.7 billion to $3.6 billion.

5.22 Despite this decrease in the size of the federal Crown corporation sector, such corporations continue to be important in the infrastructure of the Canadian economy. Many have a significant position in the sector of the economy in which they operate. Examples include Canada Mortgage and Housing Corporation, Canadian National Railway Company and Petro-Canada.

PARENT CORPORATIONS SCHEDULED AND DESCHEDULED
SINCE SEPTEMBER 1984

Scheduled	**Date**	**Notes**
Halifax Port Corp.	Dec.1984	
Port of Quebec Corp.	Dec.1984	Formerly in Canada Ports Corp.
Prince Rupert Port Corp.	Dec.1984	
Canada Harbour Place Corp.	Dec.1984	
International Centre for Ocean Development	Feb.1985	
Canada Museums Construction Corp. Inc.	Jul. 1985	
St. John's Port Corp.	Dec.1985	Formerly in Canada Ports Corp.
Marine Atlantic Inc.	Dec 1986	Former CN Subsidiary
Saint John Port Corp.	Feb.1987	Formerly in Canada Ports Corp.
Enterprise Cape Breton Corp.	Dec.1988	
Descheduled		
Northern Transportation Company Ltd.	Jul. 1985	Privatized (Jul. 1985)
Pêcheries Canada Inc.	Apr. 1986	Privatized (Apr. 1986)
Uranium Canada Ltd.	Mar. 1986	Dissolved (Dec. 1985)
Canadian Arsenals Limited	May 1986	Privatized (May 1986)
Canadian Sports Pool Corporation	Sep. 1986	Dissolved (Jun. 1985)
Loto Canada Inc.	Sep. 1986	Dissolved (Jul. 1985)
St. Anthony Fisheries Limited	Aug. 1987	Dissolved (Mar. 1987)
Societa a responsibilita limitata Immobiliare San Sebastiano	Sep. 1987	Dissolved (Dec. 1985)
Canagrex	Oct. 1987	Dissolved (Oct.1987)
Northern Canada Power Commission	May 1988	Transferred to territorial governments (May 1987)
Air Canada	Oct. 1988	Partially privatized (Oct.1988)
Teleglobe Canada*	-	Assets sold (Apr. 1987)

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* Teleglobe Canada still exists as the conduit for repayment of certain obligations to financial institutions.

Exhibit 5.2

The Framework for Control and Accountability

The legislation clarified roles and responsibilities and sets up several control and accountability mechanisms

5.23 The government's intentions in amending the Financial Administration Act were described in a statement by the President of the Treasury Board that accompanied the draft legislation when it was introduced in the House of Commons (Treasury Board of Canada: "New Legislative Proposals for the Control and Accountability of Crown Corporations";

statement by the Honourable Herb Gray, President of the Treasury Board, March, 1984). The key principles of the framework were to be:

- application to all scheduled parent Crown corporations and, through them, to their wholly owned subsidiaries;
- clarification and articulation of the responsibilities of Parliament, the government, appropriate ministers and boards of directors;
- Parliament's approval of the creation, mandate, financing and disposal of every parent Crown corporation;
- a systematic and timely flow of pertinent information to Parliament to allow it to judge whether Crown corporations are meeting their stated objectives for each planning period, and to hold the government to account;
- government responsibility for the strategic and budget decisions of all parent Crown corporations, and through them, those of their wholly-owned subsidiaries, as well as for directives issued to parent corporations; and
- a rigorous audit regime comprising internal audit, annual external audit and a periodic external special examination.

5.24 In putting these principles into effect, the legislation clarified roles and responsibilities on the one hand and set up a number of control and accountability mechanisms on the other. Exhibit 5.4 describes in summary form the interrelationships among the key mechanisms and the roles and responsibilities of the main players, as established by the legislation.

The Role of Parliament

The legislation stipulates the information that must be submitted to Parliament

5.25 With respect to Crown corporations, as in other matters, it is Parliament's responsibility to scrutinize and authorize the expenditure of public funds and to hold the government to account for achieving the associated public policy objectives. The legislation provides for the following to be laid before each House of Parliament:

- summaries of the corporate plans and capital budgets of all scheduled parent Crown corporations;
- summaries of the operating budgets of parent corporations named in Part 1 of Schedule III;
- annual reports of parent Crown corporations;
- quarterly and annual reports of the President of the Treasury Board; and
- Governor in Council directives issued to Crown corporations.

5.26 In addition, the Governor in Council may require a wholly owned subsidiary to comply with any provision of Part X as if it were a parent Crown corporation. To date, this has been applied to require the three subsidiaries of Canada Lands Company Limited and Petro-Canada International Assistance Corporation (a wholly owned subsidiary of Petro-Canada) to report as if they were parent corporations (see Exhibit 5.3).

PROFILES OF CROWN CORPORATIONS – FINANCIAL YEARS ENDING ON OR BEFORE 31 JULY 1985 AND 1988

	1985				1988			
	Employees	**Assets**	**Liabilities**	**Budgetary Funding**	**Employees**	**Assets**	**Liabilities**	**Budgetary Funding**
			($ Million)				**($ Million)**	
Schedule III – Part 1								
Atlantic Pilotage Authority	82	1.7	1.8	0.1	66	2.0	2.0	0.4
Atomic Energy of Canada Limited	6767	1225.7	1077.5	325.5	4892	1036.3	828.9	175.4
Canada Deposit Insurance Corporation	16	1360.6	2232.0	0.0	45	735.1	1842.7	0.0
Canada Harbour Place Corporation	57	88.3	11.8	48.1	11	71.0	0.4	2.0
Canada Lands Company Limited	130	16.0	16.0	66.7	0	0.0	0.0	0.0
Canada Mortage and Housing Corporation	3700	10277.0	10227.0	1728.0	3029	9540.1	9490.1	1472.9
Canada Museums Construction Corporation Inc.	32	50.1	5.3	31.5	25	249.9	23.8	68.8
Canada Post Corporation *	62477	2369.9	768.4	580.5	49108	2574.0	961.9	442.6
Canadian Commercial Corporation	120	380.9	344.6	17.6	94	606.3	576.9	11.8
Canadian Dairy Commission	78	304.0	317.6	303.6	70	212.2	212.2	287.0
Canadian Livestock Feed Board	25	2.9	2.2	18.6	21	2.1	1.9	18.6
Canadian National (West Indies) Steamships, Ltd.	0	1.0	0.4	0.0	0	1.2	0.3	0.0
Canadian Patents and Development Limited	27	1.3	0.6	0.4	26	1.2	0.7	1.1
Canadian Saltfish Corporation	53	14.5	17.8	0.0	44	27.6	33.0	0.0
Cape Breton Development Corporation	3582	397.1	62.0	107.6	3435	625.4	76.9	101.4
Defence Construction (1951) Limited	200	1.2	4.3	14.5	197	2.0	4.9	13.6
Export Development Corporation	577	6611.4	5756.9	0.0	498	6932.7	6033.3	0.0
Farm Credit Corporation	635	4940.2	4811.1	10.3	560	4307.2	4943.8	15.0
Federal Business Development Bank	1280	1566.1	1364.0	31.1	1202	2294.1	2018.0	77.8
Freshwater Fish Marketing Corporation	410	25.0	23.4	0.0	285	23.6	23.6	0.0
Great Lakes Pilotage Authority, Ltd.	148	4.3	6.5	0.3	115	4.6	6.6	1.0
Harbourfront Corporation	230	18.3	18.1	20.9	145	42.4	3.7	0.0
International Centre for Ocean Development	0	0.0	0.0	0.8	30	0.2	0.2	6.4
Laurentian Pilotage Authority	312	5.1	5.2	1.5	289	5.4	6.0	1.5
Marine Atlantic Inc.					1957	335.0	337.8	147.0
National Capital Commission	850	428.7	51.4	97.1	806	319.7	33.9	103.0
Pacific Pilotage Authority	152	4.4	1.8	0.0	61	4.5	1.9	0.0
Standards Council of Canada	75	5.3	0.9	6.6	69	1.7	1.0	6.5
St. Lawrence Seaway Authority, The	1142	696.5	350.0	7.4	985	603.0	26.2	24.5
VIA Rail Canada Inc	3653	749.8	141.0	473.5	5726	953.9	185.2	536.0
** Canada Lands Company (Le Vieux-Port de Montreal) Ltd					22	0.9	0.9	3.4
** Canada Lands Company (Mirabel) Ltd.					24	2.7	2.7	5.3
** Canada Lands Company (Vieux-Port de Québec) Inc.					12	1.7	1.5	5.1
** Petro-Canada International Assistance Corporation					28	2.7	2.7	67.4
	86810	31547.3	27619.6	3892.2	73877	31522.4	27685.6	3595.5

* Canada Post Corporation became a Schedule III - Part 2 corporation on 1 June 1989

** Subsidiaries required to report as parents

Exhibit 5.3

PROFILES OF CROWN CORPORATIONS - FINANCIAL YEARS ENDING ON OR BEFORE 31 JULY 1985 AND 1988

	1985				1988			
	Employees	Assets	Liabilities	Budgetary Funding	Employees	Assets	Liabilities	Budgetary Funding
		($ Million)				($ Million)		
Schedule III - Part 2								
Canada Development Investment Corporation	9287	678.6	1387.4	550.0	1011	284.5	58.2	0.0
Canada Ports Corporation	517	245.1	139.5	35.0	76	95.4	6.7	2.1
Canadian National Railway Company	66234	7466.6	4142.3	171.0	49317	7593.6	4492.5	20.7
Halifax Port Corporation	55	58.3	36.1	0.6	88	62.0	6.8	0.0
Montreal Port Corporation	700	237.2	259.3	0.0	673	227.4	28.4	0.0
Petro-Canada	6697	9055.3	4478.7	71.7	8517	8453.0	4581.0	0.0
Port of Quebec Corporation	123	83.6	3.9	0.0	125	67.9	4.0	0.0
Prince Rupert Port Corporation	12	79.6	89.6	1.2	12	84.2	49.4	0.0
Royal Canadian Mint*	641	72.4	71.4	0.0	832	127.4	126.3	0.0
Saint John Port Corporation					84	91.5	43.5	0.0
St. John's Port Corporation					18	15.6	3.4	0.0
Vancouver Port Corporation	230	221.0	122.4	0.0	200	251.5	16.0	0.0
	84496	18197.7	10730.6	829.5	60953	17354.0	9416.2	22.8
Total (Schedule III corporations)	171306	49745.0	38350.2	4721.7	134830	48876.4	37101.8	3618.3

* This was a Schedule III - Part I corporation in 1985

Exempt (Unscheduled) Corporations								
Canada Council	N/A	97.3	24.9	72.6	231	166.2	166.2	96.9
Canadian Broadcasting Corporation	N/A	691.0	434.2	905.0	10598	799.4	291.9	887.0
Canadian Film Development Corporation	N/A	12.2	3.9	46.6	135	27.3	7.4	115.6
Canadian Institute for International Peace and Security	N/A	1.3	0.1	1.5	24	1.8	0.2	4.0
Canadian Wheat Board, The	N/A	5029.8	5029.8	121.0	464	4835.7	4835.7	245.0
International Development Research Centre	N/A	20.3	12.3	81.0	438	24.3	15.7	108.1
National Arts Centre Corporation	N/A	14.1	14.5	15.5	325	7.3	5.7	14.9
Total (excludes Bank of Canada)		5866	5519.7	1243.2	12215	5862	5322.8	1471.5

N/A - Not Available

SOURCE: Public Accounts, Volume III, Table I

Exhibit 5.3

The legislation accords Parliament a direct role in the control and accountability framework

5.27 The role of Parliament in the control and accountability framework is not limited to questioning the government and holding it accountable, or to voting the Estimates through which operating subsidies, loans and advances are made to Crown corporations. The legislation accords Parliament a direct role in authorizing the creation or acquisition of parent Crown corporations, their disposal or dissolution, and the objects and purposes that the corporations pursue. In these respects as well as others, the availability of complete, timely and reliable information underpins Parliament's ability to exercise its responsibilities.

MAIN ELEMENTS OF CROWN CORPORATION CONTROL AND ACCOUNTABILITY FRAMEWORK

	Parliament	Governor in Council	Treasury Board	Minister	Board of Directors
Plans/Budgets					
- Corporate Plan		Approve		Recommend (2)	
- Operating Budget			Approve	Recommend	
- Capital Budget			Approve	Recommend (2)	
- Summaries of Plans/ Budgets	Receive			Approve	
Reports					
- Corporate Annual Report	Receive				
- Annual Consolidated Report	Receive		Prepare		
- Quarterly Report on Tabling	Receive		Prepare		
Directives	Receive	Approve		Recommend	Advise
Creation, Acquisition, Disposal, Dissolution					
- Parents	Approve				
- Subsidiaries		Approve			
Appointments					
- Directors		Approve		Appoint	
- Officer-Directors		Appoint			Advise
- Officers					Appoint
- Auditors of parent		Appoint			Advise
Audits					
- Internal Audit					
- Annual Audit (Report)	Receive (1)			Receive	
- Special Examination (Report)					Receive

(1) Included in the corporate annual report.

(2) The recommendation of the Minister of Finance may also be required in certain cases; for example, where significant borrowings are proposed.

Exhibit 5.4

The Role of Government

The legislation assigns to the government the key responsibilities for control of Crown corporations

5.28 Exhibit 5.4 shows the more important responsibilities assigned by Part X to the government; that is, the Governor in Council (i.e. Cabinet), the Treasury Board, the Minister of Finance and the appropriate minister. These include:

- **Plans and budgets.** There were control processes relating to operating and capital budgets before Part X was introduced. However, now there is a new requirement for all parent Crown corporations to submit multi-year corporate plans annually for Cabinet approval on the recommendation of the appropriate minister. This requirement is central to the entire control and accountability regime. It is through the corporate plan that a corporation's objectives and strategies are approved by the government -- and a benchmark is established against which subsequent performance can be assessed.

- **Directives.** The Governor in Council may issue a binding directive to a parent Crown corporation if it deems it in the public interest to do so. This is done on the recommendation of the appropriate minister, after the minister has consulted the board of directors with respect to the content and potential effect of the directive. It was anticipated from the outset that this power would likely be used sparingly -- and subsequent practice has borne this out. In practice, the government has many other formal and informal means to direct a corporation.

- **Transactions concerning subsidiaries.** Some transactions of a parent Crown corporation or a wholly owned subsidiary require Governor in Council approval. These include the incorporation or acquisition of a subsidiary; the dissolution or amalgamation of a wholly owned subsidiary; and the sale or other disposal of shares or assets of a wholly owned subsidiary. Part X does not require Governor in Council approval for changes in the mandate of a wholly owned subsidiary. Instead, the mandates of subsidiaries are controlled through a provision prohibiting them from carrying on any business that is not consistent with the objects and purposes of the parent corporation.

- **Appointments.** According to the legislation, the Governor in Council controls the key corporate appointments in a parent Crown corporation. Directors are appointed by the appropriate minister with Governor in Council approval. It is up to the Governor in Council to appoint, and remove, the Chairman, the Chief Executive Officer and any director who is also an officer of the corporation and to fix their remuneration.

The Crown Corporations Directorate has played an important role in implementing the legislation

5.29 The responsibilities Part X assigned to the government (and particularly to the Cabinet, the Treasury Board and the Minister of Finance) required the role of central agency officials to be strengthened. Although it is not explicitly provided for in the legislation (and not illustrated in Exhibit 5.4), the Crown Corporations Directorate, which reports jointly to the Department of Finance and Treasury Board Secretariat, has played an important role in implementing the legislation.

5.30 This Directorate, established in 1984 from groups that had been working on Crown corporation matters separately in Finance and the Treasury Board Secretariat, is the primary means by which the government co-ordinates the management of its Crown corporations. The Directorate serves as the "keeper of the system" and provides advice to Treasury Board ministers and the Minister of Finance on policy issues related to Crown corporations, as well as on their resources, activities and performance. During the period under review, it has put in place the main processes called for by Part X and has co-ordinated those processes with others (such as specific approvals sought through Treasury Board submissions, Cabinet memoranda and the Estimates) that affect the control and accountability of Crown corporations.

The Role of Crown Corporations

The role of the board of directors differs considerably from that of a private sector board

5.31 As a general principle of corporate law, a corporation is represented by its board of directors. Thus, when Part X (or any other relevant legislation) imposes a duty on a Crown corporation, the duty is in fact imposed on the board of directors unless another player is specified. This point is emphasized in Part X by the statement that the board of directors is responsible for managing the businesses, activities and other affairs of the corporation. Part X also sets out the duties, responsibilities and conflict-of-interest provisions applying to Crown corporation directors, in much the same way as they are defined for directors of private sector corporations in the Canada Business Corporations Act.

5.32 Nevertheless, the formal role assigned to the board is relatively circumscribed. In many respects it is a consultative role. For example, the appropriate minister is required to consult the board of directors in advance about proposed directives, the appointment of officer-directors and the appointment and removal of auditors. Unlike the private sector, the board of a parent Crown corporation controls neither the appointment nor the remuneration of the Chief Executive Officer.

The legislation sets out an elaborate audit regime.

5.33 In addition to clarifying the role of the board of directors, Part X sets out an elaborate and innovative audit regime for Crown corporations. The audit provisions are described in greater detail later in this chapter.

Implementation of the Framework

Parliamentary Level

Important differences between Crown corporations and privately owned corporations

5.34 Although there are many similarities between Crown corporations and privately owned corporations, there are also important differences, including:

- **Ownership.** Government ownership represents an investment of public money on behalf of taxpayers. Unlike shareholders in private sector corporations, individual taxpayers cannot divest themselves of their "investments" in Crown corporations and put their funds to alternative uses.

- **Financing.** Expenditure of public money is authorized by Parliament and may take various forms, including equity, loans or appropriations for operating purposes.

- **Objectives.** Crown corporations have their mandates approved by Parliament and, in keeping with those mandates, are frequently charged with pursuing public policy objectives that may compete with commercial objectives or, indeed, other public policy objectives.

- **Special requirements.** Crown corporations are subject to a variety of legislative and other requirements that are not faced by private sector corporations -- for example, employment equity, official languages and access to information.

Parliament requires complete, timely and reliable information on Crown corporations

5.35 Characteristics of Crown corporations of the nature described above call for a different form of accountability than exists between private sector corporations and their shareholders. In particular, because Parliament performs some of the functions associated with ownership (such as appropriating funds, authorizing the creation, acquisition, dissolution, disposal and objects of parent corporations), the accountability of Crown corporations properly extends beyond the formal shareholder (the Crown) to Parliament. Part X recognizes this and states that "each Crown corporation is ultimately accountable, through the appropriate minister, to Parliament for the conduct of its affairs".

5.36 **Information to Parliament.** As noted earlier, the availability to Parliament of complete, timely and reliable information on Crown corporations is essential for accountability. The information to be tabled in Parliament pursuant to Part X includes:

- **Summaries of corporate plans, capital budgets and (for Schedule III-Part I corporations) operating budgets**. In accordance with regulations issued by the Treasury Board, these summaries have to be laid before each House of Parliament within 30 sitting days of the time the corporate plans and budgets are approved by the Governor in Council and Treasury Board respectively.

- **Annual reports of Crown corporations**. Annual reports are to be submitted to the appropriate minister and the President of the Treasury Board within three months of a corporation's financial year end. The minister must cause a copy of the report to be laid before each House within 15 sitting days after receiving it.

- **Annual consolidated reports of the President of the Treasury Board.** No later than 31 December each year, the President of the Treasury Board must table an annual consolidated report on the businesses and activities of all parent Crown corporations for the financial year ending on or before the previous 31 July. In practice, the government has chosen to present this report (Annual Report to Parliament on Crown Corporations and other Corporate Interests of Canada) as Volume III of the Public Accounts of Canada.

- **Quarterly reports of the President of the Treasury Board.** Within 30 sitting days of the end of each quarter, the President of the Treasury Board is required to table a report on the time of tabling, by appropriate ministers, of annual reports, and summaries of corporate plans and budgets, for Crown corporations subject to the reporting provisions of Part X.

- **Governor in Council directives.** Copies of any directives given to parent Crown corporations by the Governor in Council must be tabled within 15 sitting days after the directive is given.

The quantity and timeliness of information to Parliament has improved

5.37 **Quantity and timeliness of information.** We concluded that the quantity and timeliness of information Parliament receives has improved significantly, compared with the period before the Financial Administration Act was amended. From the perspective of Parliament and the public in general, the quantity of information available now is a far cry from the unsatisfactory state that existed when we first reported on this issue in 1976. Then there was uncertainty about even the number of Crown corporations.

5.38 The requirement to table corporate plan summaries is completely new, as is the requirement for quarterly reports on the timing of tablings. Both help instill discipline into the process. The information available in the annual consolidated report of the President of the Treasury Board is much more comprehensive than similar information available to Parliament before Part X came into effect. Means for giving more general visibility to this important information might be considered.

5.39 Exhibit 5.5 shows, for each of the last four years, the number and percentage of reports tabled within the time frames established by statute or regulation. The table shows that in 1988, 88 per cent of corporate annual reports were tabled by the deadline. In contrast, our 1982 report on the accountability of Crown corporations showed that, in 1981 and 1982, over half the annual reports were tabled more than six months after the end of the financial years involved.

5.40 The record for tabling the corporate plan and budget summaries on time is not as good as for annual reports. The data show that in 1988, 63 percent of corporate plan summaries and 52 percent of budget summaries were tabled by the statutory deadline, with another 20 percent and 19 per cent, respectively, being tabled within 30 sitting days after the deadline. There was some improvement in 1988 compared with the three previous years.

5.41 The President of the Treasury Board has written to the appropriate ministers each year since 1986, drawing their attention to the record of the previous year and urging greater compliance. Nevertheless, this is an area where there is room for further improvement. The deadlines are established by regulation and, other than in exceptional circumstances, full compliance should be expected.

The quality of information to Parliament has weaknesses

5.42 **Quality of information.** Although there has been improvement in the quantity and timeliness of information received by Parliament, the quality of information in the summaries of corporate plans and budgets, and in corporate annual reports, is uneven. Weaknesses here undermine the ultimate accountability of Crown corporations to Parliament.

5.43 The quality of corporate plan and budget summaries has improved over the four cycles (1985 to 1988) that we reviewed. Our analysis of a sample of corporate plan summaries tabled in 1988 shows that most address the key aspects of the related plans, such as objectives, strategies and performance measures for the planning period. Nevertheless, the degree of coverage varies, and some summaries do not provide a good reflection of original documents. In addition, a number of the summaries reviewed did not follow the "Guidelines for the preparation of Summaries of Corporate Plans, Capital Budgets and Operating Budgets" issued by the Treasury Board in March, 1987. We concluded that further improvements are desirable and possible.

Processes are lacking for ensuring the quality of corporate plan and budget summaries and monitoring adherence to guidelines

5.44 It is worth noting that there is no process within the government for assuring the quality and completeness of the information contained in the corporate plan and budget summaries tabled in Parliament. Nor is there a process for monitoring the extent to which the relevant guidelines have been followed.

CROWN CORPORATIONS – SUMMARY OF TIMING OF TABLINGS

Documents	Number To Be Tabled	Number Tabled Within Deadline	Per cent Tabled Within Deadline	No. of sitting days within which documents were tabled after deadline 7 or less	8-30	31 or more	Outstanding at December 31
Annual Reports							
1985	51	41	80%	-	3	-	7
1986	55	47	85%	2	-	-	6
1987	57	53	93%	2	-	-	2
1988	43	38	88%	1	-	3	1
Corporate Plan Summaries							
1985	54	26	48%	5	10	9	4
1986	57	36	63%	5	5	7	4
1987	57	28	49%	9	8	8	4
1988	51	32	63%	4	6	8	1
Capital and Operating Budget Summaries							
1985	93	39	42%	8	18	17	11
1986	106	43	41%	26	10	15	12
1987	122	50	41%	16	16	26	14
1988	107	56	52%	8	12	29	2
TOTALS							
1985	198	106	54%	13	31	26	22
1986	218	126	58%	33	15	22	22
1987	236	131	56%	27	24	34	20
1988	201	126	63%	13	18	40	4

Exhibit 5.5

Annual reports rarely state, as required, the extent to which the corporation has met its objectives

5.45 Part X requires that annual reports include, among other things, a statement on the extent to which the corporation has met its objectives for the financial year as well as such quantitative information on performance as the Treasury Board may require. Information in the annual reports in most cases does not close the accountability loop to Parliament by relating performance in the relevant period to objectives set out in corporate plan and budget summaries. Our review of annual reports showed that they rarely present explicit statements of the extent to which objectives have been met. Indeed, in some cases the objectives for the financial year in question are not presented.

5.46 Treasury Board has not exercised its right to require specific quantitative performance information in annual reports. Although in practice many corporations do include some quantitative information on performance, such information is rarely linked (or able to be linked) to objectives.

5.47 Part X provides that Treasury Board can make regulations concerning the form and content of annual reports and corporate plan and budget summaries. Although guidelines (as distinct from regulations) on the content of summaries have been issued, neither guidelines nor regulations are yet available on annual reports. At the time of our study, the Crown Corporations Directorate was drafting annual report guidelines.

Much of the information provided to Parliament during the period under review was not used explicitly

5.48 **Parliament's use of information.** As the key documents for accountability to Parliament, summaries and corporate annual reports stand permanently referred to such committees of Parliament as may be established or designated to review matters relating to the Crown corporations concerned. We looked at the work of five parliamentary committees for the period September 1984 through October 1988, to see what use they made of the information on Crown corporations referred to them. In addition, we considered any related activity of the House of Commons and the Senate in general during this period.

5.49 We concluded that, with few exceptions, neither the House of Commons nor the Senate (including committees and individual members or senators) made much explicit use of the information about Crown corporations tabled during the period under review. Nor did either House, or any of the committees we examined, review the plans and performance of Crown corporations per se. Rather, this was done as Crown corporation matters were considered in the context of a particular issue (for example, specific to a region or constituency). In those instances, the information tabled did provide relevant background information to parliamentarians.

5.50 In considering Parliament's use of the information it is important to recognize that it is through the appropriate minister that Crown corporations are ultimately accountable to Parliament. The role that Parliament has set out for itself is to see that ministers carry out their responsibilities -- not to monitor or oversee Crown corporations directly.

5.51 Therefore, the fact that the use of information appears to be limited does not necessarily indicate that the information lacks overall utility or that it does not make an important contribution to the accountability of Crown corporations. One important consequence of tabling information in Parliament is that it serves to inform the public at large about Crown corporation matters. The principal benefit to Parliament of having the information tabled, however, is the assurance that appropriate ministers have focussed on, and endorsed, the strategic orientation of Crown corporations and have reviewed their performance -- at least to the extent that the annual reports address performance. In addition, there is the discipline of having to prepare and defend the information that is imposed on the Crown corporations.

Government Level

The appropriate minister, the Governor in Council, the Treasury Board and the Minister of Finance have the key roles

5.52 **Roles and responsibilities.** As Exhibit 5.4 demonstrates, at the government level the key roles in the control and accountability framework are assigned to the appropriate minister, the Governor in Council, the Treasury Board and the Minister of Finance. A lesser, but nonetheless important, role is played by the Privy Council Office in providing technical advice on personnel and on the management of specific issues.

5.53 In carrying out this study, we interviewed senior executives in central agencies and departments, as well as Chief Executive Officers and other directors of a number of Crown corporations. With isolated exceptions, there was broad agreement among those interviewed that the general approach of the government to Crown corporations was businesslike, co-operative and mindful of the need not to interfere in day-to-day operations. Our own observations bear out these comments.

The appropriate minister has specific powers in the control and accountability framework

5.54 Appropriate ministers. The appropriate minister's role is central to the effective functioning of the control and accountability framework. The general authority and duties of a minister are reinforced by a variety of specific powers assigned by Part X. These include:

- recommending the issuing of directives;
- appointing directors, subject to concurrence by Governor in Council;
- recommending corporate plans for the approval of Governor in Council and operating and capital budgets for the approval of Treasury Board;
- tabling annual reports and summaries of plans and budgets in Parliament;
- agreeing to any borrowing by the corporation;
- receiving the annual audit report and, on an exception basis, information from a special examination; and
- receiving reports on material developments.

5.55 In essence, all important matters relating to the existence and governance of a specific corporation, such as funding, objectives, key players, and contacts with Parliament and the government, flow directly or indirectly through the appropriate minister. The general practice is that through their appropriate ministers, Crown corporations initiate, and the Cabinet, the Treasury Board and the Minister of Finance react, as appropriate. Where the latter initiate (for example, in relation to privatization activities), they do so through the appropriate minister.

5.56 The common understanding among those we interviewed was that appropriate ministers, not central agencies, are responsible and accountable for Crown corporations. It was emphasized that the appropriate ministers are the "shareholders" to whom boards of directors are accountable. The Treasury Board, supported by its officials, is responsible for the sound management of the Crown corporation portfolio, including the allocation of resources to Crown corporations, and for ensuring compliance with the Financial Administration Act.

Ministerial control generally focusses on objectives and budgets rather than on day-to-day operations

5.57 Our study confirmed that, in general, ministerial control has focussed on the broad objectives and budgets of Crown corporations through the Part X control and accountability documents, as well as on specific issues of political significance. For the most part, ministers have properly allowed their Crown corporations a large degree of operational freedom by refraining from involvement in day-to-day operations.

5.58 The degree to which ministers are supported in their role by their departmental staff varies a great deal, depending largely on the relevance of a particular Crown corporation to the policy concerns of the department. Thus, although some departments provide detailed advice to their minister on such matters as the corporate plans and budgets proposed by a Crown corporation, other departments are not consulted at all.

5.59 Governor in Council, Treasury Board and the Minister of Finance. As Exhibit 5.4 shows, the Governor in Council, the Treasury Board and the Minister of Finance have wide statutory authority to dispose of Crown corporation matters. This includes the authority to make regulations pursuant to Part X, as well as specific authority for such matters as recommending and approving corporate plans and budgets, approving borrowing, issuing directives, appointing directors and auditors, and so on.

The Crown Corporations Directorate ensures that key mechanisms are in place and functioning well

5.60 The strong role Part X assigns to the Governor in Council, the Treasury Board and the Minister of Finance has put a spotlight on the Crown Corporations Directorate (CCD), acting as the overall guardian of the framework and providing analytical and secretariat services. Although initially characterized as the "government's single window" on Crown corporations, the CCD instead views its role (as do others) as being the "single window" only for the central agencies. Within the control and accountability framework as a whole, CCD is one among a number of players in a system of checks and balances where control, responsibility and power are dispersed. In particular, CCD does not assume fundamental responsibility for specific Crown corporations, that being the domain of appropriate ministers.

5.61 Since Part X came into effect, CCD has invested considerable effort in getting the key mechanisms in place and functioning satisfactorily, and in educating and prompting other players to play their parts. In addition, it has served as an early-warning system for appropriate ministers and the government, particularly to signal potential financial difficulties, and has acted as a catalyst to initiate and organize reviews of corporate mandates. In our view, this has been an appropriate role.

Corporate plans and budgets have been timely and generally in compliance with regulations

5.62 **Corporate plans and budgets.** Corporate plans, operating budgets and capital budgets are the linchpins of the whole control and accountability regime. The planning and budgeting process provides a way to bring issues to the attention of ministers, to identify opportunities and to initiate change. The annual submission of these documents for regular, formal review by the minister, Treasury Board and Cabinet, as appropriate, allows the government to set its agenda in terms of strategies and funding. It follows that submission and approval of these documents before the commencement of the financial year to which they apply are preconditions for effective direction and control.

5.63 In this regard, there has been significant improvement compared with the period before the Financial Administration Act was amended. In that period it was not uncommon for budgets to be submitted late. In our 1982 report on the accountability of Crown corporations we noted that in that year, for example, most capital budgets had been approved after the start of the financial year. In one case, approval had not come until after the end of the year to which the budget applied. By contrast, since Part X has come into effect, there have been relatively few instances of plans or budgets not being approved before the commencement of the financial years to which they apply.

5.64 Regulations issued by Treasury Board specify not only the time within which corporate plans and budgets are to be submitted, but also their form and content. The scope of our study did not extend to a review of the quality of information in corporate plans and budgets, but we found that, in form and content, compliance with the regulations is generally good and has been improving. It is worth noting also that the Crown Corporations Directorate has established mechanisms to monitor and promote compliance with the regulations.

Corporation Level

5.65 At the corporation level, the role of the board of directors and the audit regime are important components of the overall framework for control and accountability.

The Financial Administration Act assigns certain management responsibilities to the board of directors but assigns the key powers to the government

5.66 **Boards of directors.** Part X of the Financial Administration Act explicitly assigns to the board of directors the responsibility for managing the businesses, activities and other affairs of the corporation. The legislation also spells out some of the specific aspects of such management. For example, it calls for reasonable assurance, from the corporation's management systems and practices, that assets are safeguarded and controlled, that resources are managed economically and efficiently and that operations are carried out effectively.

5.67 On the face of it, however, the powers given to the board by the Financial Administration Act are not commensurate with the general responsibility it has been assigned. As was noted earlier (and as Exhibit 5.4 indicates), the formal role of the board is relatively circumscribed. The key powers have been allocated to the government. For example, the board does not appoint the Chief Executive Officer, nor does it have the final say on corporate plans and budgets. Similarly, although the board can make, amend or repeal by-laws, in this regard also, the Governor in Council has ultimate authority.

The government generally gives boards of directors considerable scope for action and many have assumed a stronger role than might be expected

5.68 Despite the formal allocation of powers under Part X, our interviews with directors (including officer-directors, chairpersons, audit committee members and other "outside" directors), as well as with senior central agency and departmental personnel, showed that in practice the government has usually given boards considerable scope for action. It has provided strategic direction to Crown corporations and exercised its other powers sparingly.

5.69 One development that has had the effect of increasing the apparent independence of boards of directors in managing Crown corporations is the reduction in the number of public servants appointed to boards. The general practice is that public servants are not appointed as Crown corporation directors unless required by a corporation's enabling legislation. In the three year period from 1984-85 to 1987-88, the proportion of parent Crown corporations with one or more public servants on the board of directors fell from about one half to less than a third.

5.70 The end result of the way the government has used its powers is that many boards of directors, although not all, have assumed a stronger role than might be expected in managing Crown corporations. Significant aspects of that role include the following:

- The board of directors helps set the strategic direction of the corporation by reviewing management proposals and endorsing corporate plans submitted to the appropriate minister. Ultimate authority for approving the plans rests with the government, but the practice in recent years has been that most are approved without major changes. The power of the board to endorse or modify plans is thus important, as they are very likely to be accepted.

- Boards of directors monitor whether management pursues the approved strategic direction of the corporation and attains objectives. They do this on the basis of information from management and from the internal and external audit functions.

- The legislation provides that the Governor in Council is responsible for setting the remuneration, including performance pay and bonuses, of officer-directors (for example, the Chief Executive Officer). However, government guidelines issued in 1987 require boards of directors to assess annually the performance of officer-directors for purposes of making recommendations concerning remuneration. In the case of a Chief Executive Officer, for example, such assessments are based on the performance of the corporation in relation to its corporate plan, as well as the performance of the individual against pre-determined objectives.

- Boards of directors are responsible for fixing any benefits other than remuneration provided to the Chief Executive Officer, and for appointing officers other than officer-directors.

- Boards of directors set out in by-laws the duties and responsibilities of officers and officer-directors. Although Part X provides that the Governor in Council may direct the board of directors of a parent Crown corporation to make, amend or repeal a by-law, this power has not been exercised to date.

5.71 In general, we noted that the more commercially oriented and competitive a particular Crown corporation is, the easier it tends to be for the board to exercise a role broadly analogous to that of a private sector corporation's board. However, it was also evident from our interviews that the accountability chain in Crown corporations is more complex in practice than that faced by corporations in the private sector.

Few of the Crown corporation directors we interviewed had been briefed on their duties

5.72 Because of the complexity of the Crown corporation control and accountability framework, we expected to find that new directors would be thoroughly briefed on their role and duties in general, as well as on the specific corporation. However, only a few of the directors we interviewed had been briefed on their general duties as Crown corporation directors under Part X. Most believed that such a briefing would have enhanced their effectiveness. They were more likely to have been briefed on the corporation than on their duties, but here too a majority had to learn about the corporation in the course of serving on the board. The Crown Corporations Directorate has initiated a project to assess the needs of board members for briefing on their duties under Part X.

The legislation requires three types of audits -- internal audits, annual audits and special examinations -- and the establishment of audit committees

5.73 **The audit regime.** Although any audit regime (especially external audit) stands somewhat outside a control and accountability framework, it is an important element in ensuring that the framework functions as intended. Exhibit 5.6, which describes the three main types of audit called for by Part X, shows that they all relate back to the corporation's responsibility to safeguard and control its assets, manage its resources economically and efficiently, carry out its operations effectively and report on the results.

5.74 In addition to mandating the three types of audit, Part X requires that parent Crown corporations, and wholly owned subsidiaries that have separate annual auditor's reports, establish audit committees to oversee internal audits; to review and advise the board of directors about financial statements to be included in the annual report of the corporation; and to advise the board about annual audits and special examinations. An audit committee comprises at least three directors, the majority of whom are not officers or employees of the corporation or any of its affiliates Our study showed that Crown corporations generally have set up audit committees to carry out the duties defined in the legislation.

Crown corporations must carry out internal audits to assess the corporation's compliance with specific legislative provisions

5.75 Internal audit. Crown corporations must carry out internal audits to assess whether the corporation has maintained books, records, systems and practices as required under Part X (see Exhibit 5.6). An exemption from this requirement may be granted if, in the opinion of the Governor in Council, the costs of such audits would outweigh the benefits. Both the external auditor and the examiner are required to rely on internal audit to the extent they consider it practicable.

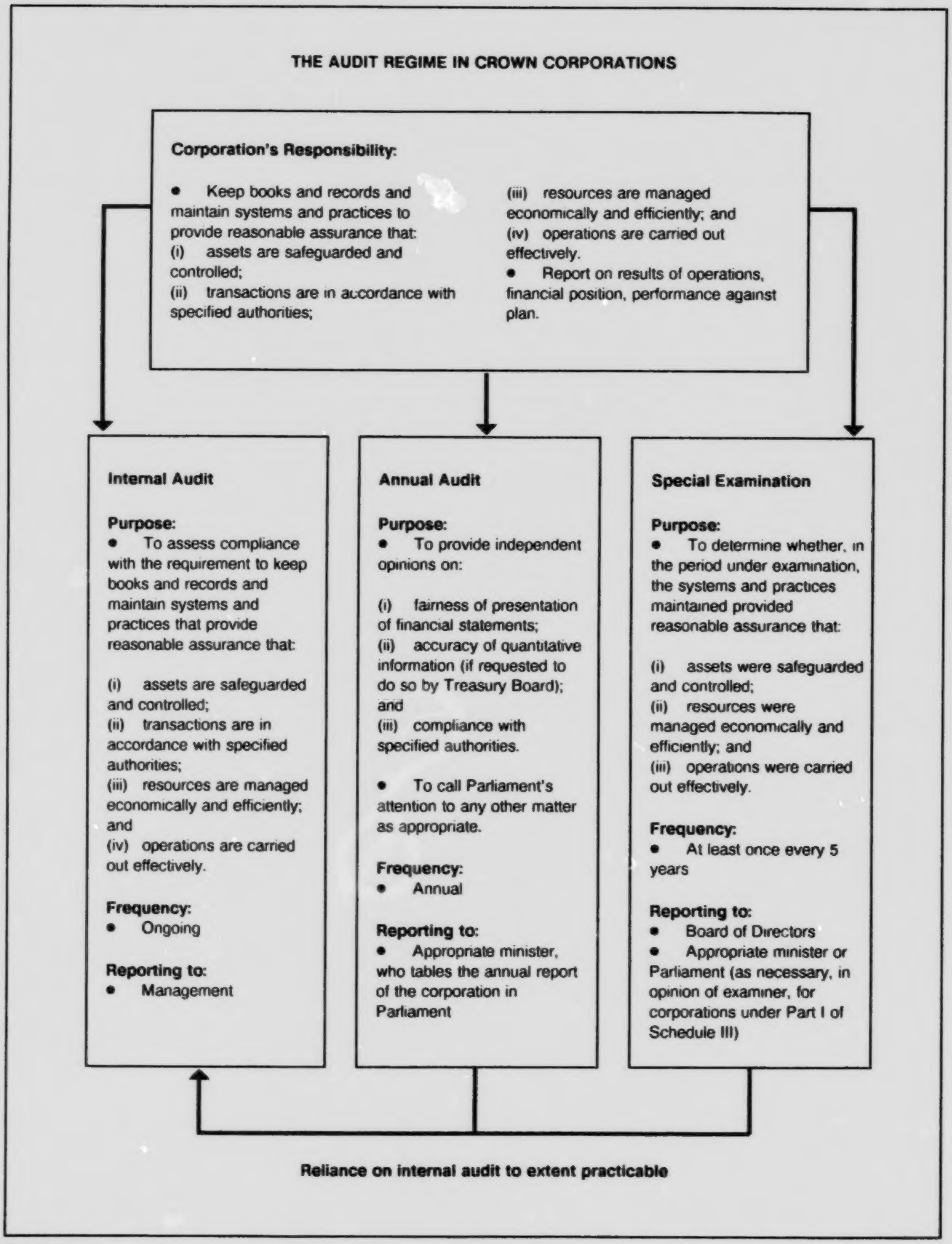
5.76 Some Crown corporations with well developed internal audit functions moved quickly to assume the internal audit responsibilities assigned by Part X In some others, however, carrying out internal audits along the lines required by Part X has gotten off to a slow start. It would be unrealistic to expect all, or even most, corporations to have implemented the new and extensive internal audit requirements in the relatively short period since Part X came into force. It takes time to build up internal audit teams and to develop the methodologies and experience required.

5.77 It is evident that some Crown corporations will be seeking exemptions from the internal audit requirement following the completion of the first special examinations. In the meantime, the Crown Corporations Directorate has developed a policy on the process for seeking and granting exemptions.

The legislation introduced some new annual audit requirements

5.78 Annual audits of Crown corporations had previously covered financial attest, "compliance with authorities" and the reporting of any "other matters". Part X introduced two new requirements.

5.79 First, there is a requirement that, if requested by Treasury Board, the auditor will provide an opinion on the accuracy, in all material respects, of any quantitative performance information in the corporation's annual report. This potentially important provision, which recognizes that a Crown corporation's financial statements seldom fully reflect its performance, has not yet been implemented.



THE AUDIT REGIME IN CROWN CORPORATIONS

Corporation's Responsibility:

- Keep books and records and maintain systems and practices to provide reasonable assurance that:
  (i) assets are safeguarded and controlled;
  (ii) transactions are in accordance with specified authorities;
  (iii) resources are managed economically and efficiently; and
  (iv) operations are carried out effectively.
- Report on results of operations, financial position, performance against plan.

Internal Audit

Purpose:
- To assess compliance with the requirement to keep books and records and maintain systems and practices that provide reasonable assurance that:

(i) assets are safeguarded and controlled;
(ii) transactions are in accordance with specified authorities;
(iii) resources are managed economically and efficiently; and
(iv) operations are carried out effectively.

Frequency:
- Ongoing

Reporting to:
- Management

Annual Audit

Purpose:
- To provide independent opinions on:

(i) fairness of presentation of financial statements;
(ii) accuracy of quantitative information (if requested to do so by Treasury Board); and
(iii) compliance with specified authorities.

- To call Parliament's attention to any other matter as appropriate.

Frequency:
- Annual

Reporting to:
- Appropriate minister, who tables the annual report of the corporation in Parliament

Special Examination

Purpose:
- To determine whether, in the period under examination, the systems and practices maintained provided reasonable assurance that:

(i) assets were safeguarded and controlled;
(ii) resources were managed economically and efficiently; and
(iii) operations were carried out effectively.

Frequency:
- At least once every 5 years

Reporting to:
- Board of Directors
- Appropriate minister or Parliament (as necessary, in opinion of examiner, for corporations under Part I of Schedule III)

Reliance on internal audit to extent practicable

Exhibit 5.6

5.80 The Crown Corporations Directorate currently receives quarterly reports on the performance of Crown corporations and uses the information to keep Treasury Board ministers briefed on developments. With the experience in developing and reporting performance indicators that has been built up in this manner over a number of cycles, the government should encourage (and even require) corporations to include such information in annual reports and ask auditors to apply the corresponding audit provision.

Our review showed that much progress has been made and that all the fundamental processes are in place. However, some points deserve further attention.

5.81 Second, Crown corporations are required to prepare their financial statements in accordance with generally accepted accounting principles (GAAP). There has been some difficulty in applying GAAP consistently across corporations in such areas as the accounting treatment of appropriations and capital and operating leases, as well as the valuation of assets and liabilities in some cases. There may be an opportunity here for the Treasury Board to exercise its power to make regulations concerning financial statements generally and, specifically, to augment or supplement GAAP so as to promote more consistent and meaningful disclosure. The Office of the Comptroller General of Canada, in conjunction with the Crown Corporations Directorate, is reviewing Crown corporation accounting practices to determine whether such guidance is necessary.

A special examination of management systems and practices is required at least once every five years

5.82 Perhaps the most significant new audit-related requirement is for a "special examination" of a parent Crown corporation and its wholly owned subsidiaries to be carried out at least once every five years -- normally by the external auditor. The purpose is to provide independent assurance to the board of directors that the corporation's systems and practices do indeed provide reasonable assurance that assets are safeguarded and controlled, resources are managed economically and efficiently and operations are carried out effectively. Although the board of directors is the primary client for the special examination, information may also be reported to the appropriate minister or to Parliament at the examiner's discretion -- but only for parent corporations named in Schedule III-Part I or their wholly owned subsidiaries.

5.83 At the time of preparing this report, it seemed probable that, with isolated exceptions, special examinations would be completed in all Crown corporations within the first five years of the introduction of Part X in September 1984.

Most directors interviewed thought the special examinations were valuable, but some thought they constituted an unnecessary expense

5.84 Our interviews with directors showed that there were mixed feelings about the value obtained from special examinations. The majority of directors interviewed saw it as an important process in helping the board hold management to account. However, in the more commercially oriented corporations, where financial statements were thought to demonstrate performance adequately, there was some questioning of the need for the corporations to bear the additional cost of a special examination. Some directors had difficulty in distinguishing the special examination from internal audit.

5.85 This Office, as the sole or joint auditor of 34 of the 44 scheduled parent Crown corporations, is carrying out an internal review of experience with the first cycle of special examinations. The primary purpose of the review is to identify ways of improving this important process in future cycles.

Can a board of directors hold the corporation's senior management to account when all board members are officers of the corporation?

5.86 We note that there are some Crown corporation boards of directors made up entirely of officers of the corporations. When the Financial Administration Act was amended, these cases were specifically recognized as exceptions to the rule that the majority of directors of a parent Crown corporation should not be officers or employees of the corporation. Nevertheless, the notion of a board of directors holding the corporation's senior management to account -- through the special examination process, among other things -- loses its meaning in these cases.

Conclusion

5.87 This review of the Crown corporation control and accountability framework accepted the Part X framework as given and focussed on the manner and extent to which it has been implemented since it was introduced in 1984. As such, the main concern was with process, rather than substantive aspects of Crown corporation control, accountability and performance. Thorough and disciplined implementation of the processes is an important first step. Until the framework has been fully implemented, it is not possible to make valid judgments about the quality of the framework itself, or its full impact on the control and accountability of Crown corporations.

5.88 Our review showed that a great deal of progress has been made and that all the fundamental processes are in place. However, some points deserve further attention. These include:

- meeting deadlines for tabling, in Parliament, corporate plan and budget summaries, and corporate annual reports;
- improving the quality of corporate plan summaries as a reflection of the corporate plans and as yardsticks for subsequent reporting of performance in annual reports;
- strengthening linkages between objectives articulated in summaries and subsequent reporting of performance in annual reports;
- briefing new directors on their duties under the Part X regime and on the Crown corporations to which they are appointed;
- assessing the need to exercise Treasury Board's right to request the audit of quantitative performance information and its right to make regulations to augment or supplement generally accepted accounting principles so as to promote more consistent and meaningful disclosure; and
- reviewing the need for exceptions from the rule that all Crown corporation boards should have a majority of directors who are not officers or employees of the corporation.

5.89 It is important to recognize, of course, that the framework, as implemented, must ultimately be judged in terms of its substantive impact. That is a subject for a future report. In the meantime, it will be important to build on the solid progress that has been made and to maintain the momentum developed during the past five years in getting the main processes in place and working well.

6

DENIAL OF INFORMATION REQUIRED TO AUDIT MINISTERS' TRAVEL EXPENSES

6

DENIAL OF INFORMATION REQUIRED TO AUDIT MINISTERS' TRAVEL EXPENSES

Main Points

6.1 In 1989-90 we had planned to conduct a government-wide audit of expenses claimed by ministers for travelling on government business. In our opinion, the Auditor General has clear statutory authority to audit these expenses (paragraphs 6.5 and 6.9).

6.2 We requested access to receipts where ministers had followed Treasury Board's advice to retain them. The Government told us that even if receipts existed they would not be made available to us (6.18 and 6.19).

6.3 We sought access to the written requests from ministers to the Minister of National Defence for use of VIP fleet aircraft. The Government indicated that we would not be provided with this information (6.36 and 6.37).

6.4 The Auditor General therefore decided that in accordance with the Auditor General Act, Section 7(1)(b), he must report to the House of Commons that he had not received all the information and explanations required to carry out the work of his Office. He also has decided not to proceed with the audit at this time (6.41).

DENIAL OF INFORMATION REQUIRED TO AUDIT MINISTERS' TRAVEL EXPENSES

6.5 In 1989-90 we had planned to conduct a government-wide audit of expenses claimed by ministers for travel on official government business, including expenses of accompanying exempt staff and public servants. Specifically, we had planned to audit:

- the adequacy of systems for financial control and reporting of ministerial office travel;
- the adequacy of controls over the use of administrative flight services (AFS or VIP Fleet) by ministers and staff, cost recovery by the Department of National Defence (DND) and the reliability and completeness of information on the operating and overhead costs of the Fleet; and
- the completeness of information on the costs of ministerial travel provided in the Public Accounts of Canada.

6.6 To verify that financial and reporting controls were working satisfactorily, in April 1989 we requested access to receipts and other documentation supporting ministers' travel expense claims. We also requested copies of requests written by ministers to the Minister of National Defence (MND) for use of the VIP fleet.

6.7 On behalf of the Government, the Privy Council Office (PCO) informed us on 13 June 1989 that the information we had requested would not be made available to the Auditor General.

6.8 Our authority to conduct the audit and the Government's reasons for not providing the information are discussed below.

In our opinion, the Auditor General has clear statutory authority to audit ministers' travel expenses.

6.9 In our opinion, the Auditor General has clear statutory authority to audit ministers' travel expenses. As stated in the Auditor General Act, the Auditor General is auditor of the accounts of Canada, including those relating to the Consolidated Revenue Fund. These include the accounts of the various departments and agencies of government.

6.10 The travel expenses of ministers are paid out of departmental budgets. The Treasury Board states in its Administrative Practices: Guidelines for Ministers' Offices:

> A ministerial budget is an integral part of a department's budget, and is subject to the same provisions of the Financial Administration Act (FAA) that apply to all other departmental funds. These provisions are intended to assure Parliamentary control over public money; they prescribe a complete financial control framework over all financial transactions.

6.11 Ministers' travel expenses are reimbursed under an honour system; supporting receipts do not have to be submitted or retained. In response to our request for access to receipts and supporting documentation for ministers' travel claims, the Government wrote that ministers do not have to submit or retain such supporting information. It stated:

> As you are aware, Ministers are required by virtue of a 1963 Treasury Board decision, only to provide a certificate stating their expenditures to secure

reimbursement. Ministers are not required to submit, nor are they required to maintain any receipts with respect to such expenditures.

6.12 We learned that this honour system had been initiated on 2 December 1963. On that date, Cabinet approved a proposal from the Minister of Finance as to how ministers should submit accounts for moneys advanced and spent for travel on official business.

6.13 For each trip ministers were asked to report expenses under two general headings -- transportation expenses and other expenses -- together with a statement of the duration of the trip and the place visited.

6.14 Ministers were required to certify that their expenditures had been incurred on official business. The certification is made pursuant to a requirement in the Financial Administration Act for a certification that "work has been performed, the goods supplied or the service rendered as the case may be". At the time of our request the Government indicated that such certificates would be made available to us.

6.15 We pointed out that in its guidelines Treasury Board had stated that:

> While, for reason of confidentiality, some payment requests by Ministers do not have to be supported by receipts and other documents that provide evidence of goods and/or services received, these supporting documents should nevertheless be retained in Ministers' offices for possible verification by, for example, the Auditor General of Canada.

6.16 We also pointed out that in its Guidelines Treasury Board had advised that "Even though Ministers do not have to provide receipts and supporting documentation, it would be prudent to maintain such information in Ministers' offices for audit purposes".

6.17 The Government wrote to us on 17 August 1989. It stated that:

> Ministers' offices have indeed been advised that it would be prudent to maintain their receipts for travel expenses. The rationale for that advice is based on the fact that Ministers are accountable to the House of Commons and would want to be in a position to respond, in the event that questions were raised in the House.

6.18 We requested access to receipts in those cases where ministers had followed Treasury Board's advice to retain receipts.

6.19 The Government told us that even if receipts existed it would not make them available to us. Only the previously mentioned certificates would be provided. It stated:

> While such certificates would, of course, be available for the proposed audit, any other receipts that may exist in the Minister's office records would not, in our view, be so available.

6.20 A system that does not require receipts to support claims for expenditures is not susceptible to audit. Without receipts we cannot determine whether claims for reimbursement are appropriate.

6.21 We also cannot make this determination if the Government will not make available those receipts kept by ministers who followed Treasury Board's advice that it would be prudent to keep receipts.

6.22 **We also wanted to audit the adequacy of the financial and reporting procedures for use of the VIP Fleet.** DND operates the Administrative Flight Service

(VIP Fleet) for members of the Royal Family, the Governor General, the Prime Minister, past prime ministers travelling for purposes related to their former office, Cabinet ministers, foreign dignitaries visiting Canada, parliamentary committees or delegates on official business and, when authorized by a minister, senior federal officers on government business.

6.23 The fleet of eight Challenger aircraft is available for use throughout the year, seven days a week, 24 hours a day. Other types of airplanes, such as a Boeing 707, are also available.

6.24 The VIP Fleet is supposed to be used only under certain conditions. The Guidelines state that "Executive aircraft should only be used in cases where commercial air service is not available or not suitable, and when the purpose of the trip is to carry out ministerial or departmental business." Further, the Guidelines state that "These aircraft may never be used for party or constituency purposes, or for purposes connected with an election campaign".

6.25 Specifically, the aircraft are supposed to be used by ministers in the following circumstances:

- When the flight is being made to a point where there is no commercial air service; where no space is available on a commercial air service; or where, because of difficulties in routing or timetables, substantial savings of essential time can be made by using administrative aircraft in place of commercial services.
- When sudden changes in plans require emergency air transportation.
- In instances where ministers are travelling with official parties of some size that need to travel together and where advantage can be gained by using a government aircraft.
- Where security considerations render commercial travel impractical.

6.26 The minister requesting use of the VIP Fleet is supposed to follow specific procedures which include stating the specific reasons for use. According to the Guidelines, the office of the minister requesting a flight is expected to telephone DND with a preliminary indication of the requirement and the reason for the request. The request is then passed to the Flight Co-ordination Centre in DND, which contacts the minister's office to obtain necessary details.

6.27 The minister requesting the flight is also required to forward a written request for the flight to the Minister of National Defence providing:

- an itinerary of the trip, which indicates all points of departure and arrival;
- the specific reason(s) for which the use of government-owned aircraft is requested;
- a complete list of passengers showing their departure and arrival points and their affiliations; and
- the contact person in the requesting minister's office.

6.28 In addition, the following statement must be included:

"I (or my Minister) request(s) the use of this aircraft, fully cognizant of the Guidelines for Use of the AFS, consistent with the Government's commitment to restraint, and consistent with the Conflict of Interest and Post Employment Code for Public Office Holders."

6.29 The request must be signed by the minister requesting the flight or by the minister's executive assistant on behalf of the minister.

6.30 **Charges to ministers for use of VIP Fleet vary according to type of flight.** In 1984 the Secretary to the Cabinet wrote to ministers and deputy ministers concerning the use of the VIP Fleet. He indicated that the Prime Minister had approved the procedures outlined in the memorandum.

6.31 The memorandum identified three types of executive flights:

> Special Flight is defined as a flight carrying members of the Royal Family, the Governor General or the Prime Minister.
>
> Ministerial or Parliamentary Flight is a flight arranged by the Governor General, the Prime Minister, a Minister of the Crown, the Speaker of the House of Commons or the Senate, or delegations on official business, foreign heads of state and visiting dignitaries and such other persons as may be authorized, for general government purposes not specifically related to the programmes of a department.
>
> Departmental Programme Flight is a flight involving a minister, a minister with officials, and such other persons as may be authorized by a minister or officials travelling alone on business related to a departmental programme.

6.32 The memorandum also outlined the costs to be charged to the requesting minister for the different types of flights:

> Special Flight: No charges.
>
> Ministerial or Parliamentary Flight: Double the first class return fare per flight that would be charged by commercial carriers for the same or similar flight, or $100, whichever is greater. This charge is per flight, not per person.
>
> Departmental Flight: Charges are recovered in accordance with rates approved by the Treasury Board.

6.33 The minister requesting the flight decides how it will be categorized.

6.34 For Fiscal year 1989-90 the departmental flight charge for a Challenger aircraft is $2,451 per flying hour. These charges do not include in-service maintenance costs, attrition, depreciation, base support and crew costs. Based on 1989-90 data from DND, adding these costs would increase the charge to about $5,460 per hour, or by 123 percent. The actual costs of a given flight would also include the cost of food and amenities ordered by the travelling minister for all passengers and an adjustment for the actual travel expenses of the airplane crew.

6.35 Our initial audit survey found that about 95 percent of flights are categorized by the requesting minister as Ministerial or Parliamentary flights, which means that ministers are usually charged at the lowest rate. For example, $3,815.20 or double the first class fare was charged for one recent flight. If charges had been at the departmental program flight rate the cost would have been about $29,900. The addition of

The Auditor General then decided that, in accordance with the Auditor General Act, Section 7(1)(b), he must report to the House of Commons that he had not received all the information and explanations required to carry out the work of his Office.

non-included costs would have increased the flight charges to an estimated $66,600. The full costs of operating the VIP Fleet, either in total or for each minister, are not disclosed to Parliament. However, DND has advised us that it is bound by the provisions of the Access to Information Act and rarely, if ever, has grounds for withholding cost information.

6.36 We were denied access to information on the purposes for the use of the VIP Fleet by ministers. We sought access to the written requests from ministers to the MND for use of VIP Fleet aircraft, to verify that aircraft were being used for official business and under the conditions stipulated in the Guidelines, and that the charges to ministers for use of the aircraft were appropriate.

6.37 In its letter of 13 June, the Government indicated that we would not be provided with this information.

6.38 Conclusion: We believe that Parliamentary control over the public purse extends to travel expenditures made by ministers on official government business. We found that the full costs of operating the VIP Fleet, either in total or by minister, are not disclosed to Parliament.

6.39 An audit by this Office is an integral component of maintaining Parliamentary control.

6.40 We reviewed whether or not we should proceed with an audit, given that:

- Ministers' claims for travel expenses are reimbursed under a system that is not susceptible to audit because supporting receipts do not have to be submitted or retained.
- Even if ministers kept receipts, based on Treasury Board's advice to be prudent, the receipts would not be made available to us.
- Information on the purposes for use of the VIP Fleet by ministers would not be made available to us, which would prevent us from determining whether use was for official government business only and that the charges for use were appropriate.

6.41 The Auditor General then decided that, in accordance with the Auditor General Act, Section 7(1)(b), he must report to the House of Commons that he had not received all the information and explanations required to carry out the work of his Office. After careful consideration, he also decided that we would not proceed with the audit at this time.

7

EFFICIENCY

The Management and Use of Telecommunications in the Federal Government

7

EFFICIENCY

The Management and Use of Telecommunications in the Federal Government

Main Points

7.1 This year we examined how efficiently the federal government uses its telecommunications services. In 1962, the Royal Commission on Government Organization (Glassco Commission) emphasized the importance of co-ordinating departments' use of voice communications. We believe the same is true today for data communications. However, savings from economies of scale by combining voice communications links were not being pursued by the government in 1962 and are not being pursued for data communications 27 years later (paragraphs 7.8 to 7.16).

7.2 We estimate the short-term potential for government-wide savings in data communications to be between 20 and 30 percent of operating expenditures. This translates into annual savings of $30 million to $45 million, based on current data communication operating expenditures of $150 million. In the longer term, we estimate that additional savings of at least 15 percent of voice operating expenditures are achievable with the integration of voice and data on government-wide networks (7.17 to 7.21).

7.3 We believe that, to achieve these potential savings, a central focus is required for government-wide administration of both voice and data communications as a common service, through a responsible body, such as a common service agency, held accountable to achieve an efficient and cost-effective telecommunications service (7.22).

7.4 The Treasury Board and the Department of Communications have taken little action to enforce a common service agency role for the efficient management of telecommunication services on a government-wide basis. Departments have no reason to consider anything more than their own requirements, resulting in a proliferation of parallel networks across the country. With no clear leadership, the government is not positioned to take advantage of either the significant existing opportunities or the technological innovations that should soon be available (7.23 to 7.38).

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EFFICIENCY

The Management and Use of Telecommunications in the Federal Government

Introduction

Audit Objective and Scope

7.5 Data and voice telecommunications are rarely given the same level of emphasis and attention as the more visible computer hardware and software products. However, the federal government spends a surprising $1 billion annually for telecommunications goods and services. These goods and services form an essential component of many of the information systems used by departments for program delivery and administration.

7.6 Our examination addressed the way departments use telecommunications services. Our audit objective was to identify opportunities for realizing significant savings in voice and data communications expenditures. We focussed on the policies and practices of five major user departments, the activities and role of the Government Telecommunications Agency (GTA), and the role of central agencies.

7.7 The five departments selected were:

- Agriculture
- Employment and Immigration (CEIC)
- Environment (DOE)
- Public Works (DPW)
- Supply and Services (DSS)

The $1 Billion Government Telecommunications Environment

Today's management of data communications mirrors the fragmented management of voice communications in 1962

7.8 We estimate, on the basis of forecasts for 1988-89, that the federal government spends in the order of $1 billion annually for telecommunication goods and services. Approximately 48 percent, or $490 million, is for operations, primarily the lease of common carrier services. The remaining 52 percent, or $540 million, is for capital expenditures. Of the $490 million for operations, almost 70 percent represents voice traffic (telephones) and 30 percent data traffic. Departments purchase $320 million in services directly from the common carriers of which $70 million is arranged through the Government Telecommunications Agency (GTA). GTA provides the remaining $170 million in services and bills departments for them.

7.9 Exhibit 7.1 shows the growth in telecommunications operating expenditures in the past 10 years. In coming years, the most significant area of growth will be data

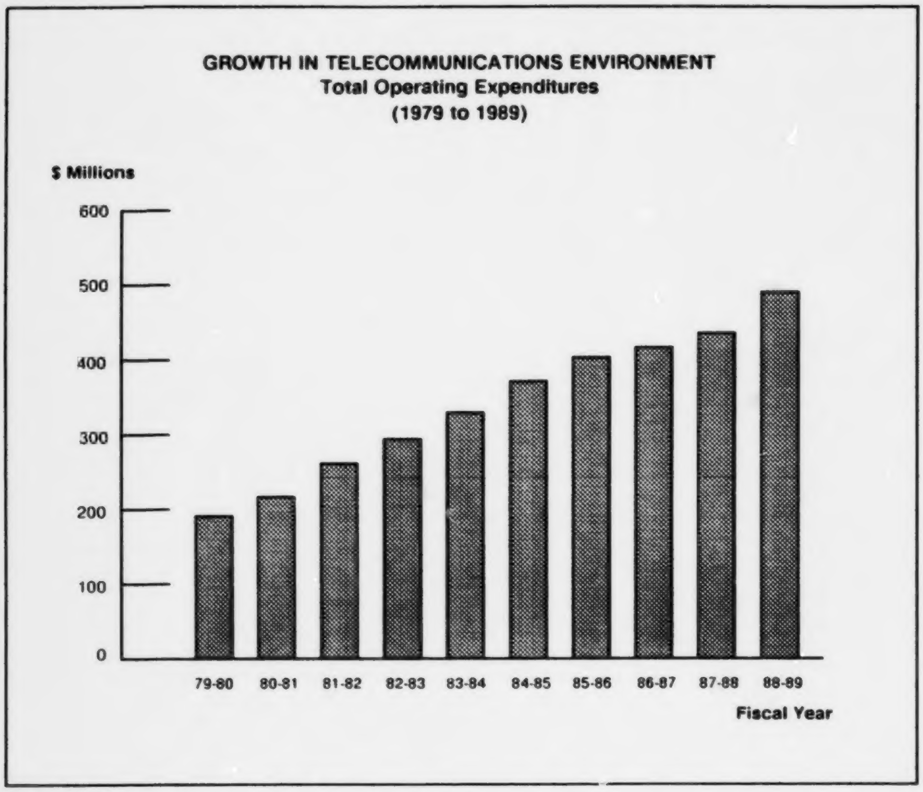

Exhibit 7.1

communications. The common carriers estimate that industry-wide data traffic will increase by at least 15 percent a year on a compounded basis.

7.10 In 1962, the Royal Commission on Government Organization (the Glassco Commission) recommended the establishment of a Government Telecommunications Agency. At that time, total government telecommunication expenditures -- for voice and teletype -- were $50 million annually. The Glassco Commission expressed several major concerns of direct relevance to our audit. One of these addressed the potential savings from pooling and integrating departmental requirements:

> . . .a single co-ordinating agency must be created with responsibility to assist departments in achieving suitable standards of communications performance, eliminating duplication of facilities and initiating such integration and pooling of services as will promote the realization of the important economies which are possible.

Significant savings are realized through government-wide management of voice communications

7.11 Voice communications conform to standard, carrier-provided services. We found that, within this environment, GTA provides an efficient inter-city voice service for departments and agencies by administering a private "Intercity Network" on circuits leased from the common carriers. This network makes possible savings in the area of 40 percent over the direct distance dialing daytime rates for message toll service. All the departments we examined use the Intercity Network to take advantage of the potential economies of scale. The network results in annual savings to the government estimated by GTA to be approximately $43 million.

7.12 In voice telecommunications, most departments demonstrate concern for minimizing costs. The use of GTA's intercity voice network creates efficient use of voice communications, where departments have access to it.

The complexity of data communications demands more active government-wide co-ordination

7.13 The federal government does not receive any preference in rates, which would be viewed by the Canadian Radio-television and Telecommunications Commission (CRTC) as a discriminatory practice. Regulated telecommunications rates apply to all users. However, the CRTC recently set a precedent by approving a discount based on guaranteed volumes of traffic for a packet switched service. This tariff filing was a made in response to GTA's requirement for such a service. The Government Packet Network (GPN) takes advantage of this volume discount opportunity. GTA has "bulk-purchased" capacity, enabling users of the GPN to obtain a 20 percent discount on rates. The government-wide data traffic was estimated by GTA to be sufficiently large to guarantee enough volume to secure this discount. However, by the time GTA had established the GPN many departments had already developed and implemented their own networks and chose not to switch to the GTA service. Although the GPN's current volume is sufficient to maintain the 20 percent discount, the service is not fully utilized. Therefore, the full cost savings potential of the GNP that can be realized through wider government use is not being achieved.

The federal government spends $1 billion annually for telecommunications goods and services, which are essential for program delivery and administration.

7.14 Most departments with significant data communication requirements have developed private networks to meet their own specific needs. These private networks were seldom developed with active GTA participation or consultation. Where departments had contacted GTA, for example to develop AgriNet, CEINet and UIT, GTA's involvement was minimal. While each department appears to meet its individual needs reasonably efficiently, together they are losing significant cost-saving opportunities by not having a government-wide efficiency perspective. With little central focus or incentive to ensure that a government-wide perspective is emphasized, departments have given little consideration to achieving government-wide efficiencies in telecommunications.

7.15 In all the departments we examined we observed cross-country data links that had developed independently from other departments with similar traffic routes. As a result, departments have created many parallel networks that are more costly and inefficient because of their smaller volume.

7.16 This multiplicity of private data communications networks is inefficient. Many of these parallel networks link regional offices in the same cities to Ottawa, with more expensive, lower speed data circuits. This results in duplication of the capital investment in modems, multiplexers and switches and in the lease of relatively high-cost, low speed circuits.

7.17 It is difficult to calculate the total potential savings because of the large number of different networks and the lack of government-wide data traffic forecasting or analysis. However, our estimates, which we believe to be conservative, show potential savings of 20 to 30 percent of data communications operating expenditures annually. On current operating expenditures of approximately $150 million, savings of between $30 million and $45 million could be achieved in the first year of full data consolidation. The potential for such annual savings will continue to increase as the total use of telecommunications by the government increases.

7.18 The potential for total telecommunications savings falls under four major headings:

- savings by multiplexing individual data networks into a few high-speed networks that enable the government to take greater advantage of existing tariff structures;
- more efficient use of the existing circuits;
- person-year savings in individual departments through organizational rationalization; and
- savings achieved by integrating voice and data services.

7.19 Within approximately five years, we estimate that further savings of 15 percent of total operating expenditures will be attainable through the integration of voice and data services. Not taking action now to improve the structure of data communications in the federal government will result in considerable additional downstream costs. We believe that the significance of future benefits derivable from new technologies will eventually force the government to address its telecommunications operations. The savings currently available in data transmission, as discussed above, will also be available in voice transmission if the government pursues the integration of voice, data and other telecommunication services. To minimize downstream expenses and to take advantage of the full potential savings, the government will have to take a consolidated approach to satisfying departmental data traffic needs.

7.20 We found that planning for data services is done by individual departments, which generally does not take advantage of the potential benefits of a common service approach. Although the planning for such services is not well documented, we found evidence that departments were striving for improved efficiency within the limited view of departmental needs.

7.21 It is disappointing to note the similarities between the deficiencies in the management of voice communications reported by Glassco in 1962, and the problems in the current data communications management environment. The message in both cases is that the government is not pursuing the benefits that could be derived from economies of scale.

7.22 To achieve the significant savings that are attainable, we believe that a central focus is required for government-wide administration of both voice and data communications as a common service, through a responsible body such as a common service agency, held accountable to achieve an efficient and cost-effective telecommunications service.

The government has failed to take advantage of significant opportunities to reduce costs by combining departmental traffic into government-wide networks

7.23 Combining departmental data traffic would allow for more efficient use of switching and transmission facilities and would enable the government to benefit from lower unit costs. Combining separate transmission needs would lead to better use of available network capacity and would allow the government to take advantage of a sliding price scale for data speed costs (costs per bit per second decrease as circuit capacity increases). Larger capacity, and therefore fewer, lines could be leased from carriers to meet the planned needs of departments. Technology developments have made it possible to increase efficiency in telecommunications through the use of broadband capacity for voice and data traffic. A single, high-capacity "pipe" can be leased on which many voice and data circuits can be multiplexed. Such an approach would also take advantage of variations in demand and lower unit costs. These are options that the federal government telecommunication managers could be pursuing.

7.24 Savings can also be achieved with better planning and co-ordinating of networks within the government. Activities like data traffic forecasting, which common carriers and major users of telecommunications services regularly undertake to support their planning and operations, are not done on a government-wide basis. This restricts GTA's ability to identify overall government volume and take advantage of potential cost saving opportunities. With better knowledge of operations and government-wide potential, a common service agency could plan for and negotiate more efficient communications services. As volumes of traffic become large enough, other options such as high speed data services become viable alternatives where the greatest potential exists for cost savings.

7.25 Exhibit 7.2 shows that as data traffic is combined, other options become available that offer more cost-effective service to the government as a whole, at reduced tariff rates. We found that the departmental data communication links operate at low data speeds (9.6 to 56 Kbps). Combining data traffic to obtain larger single volumes would permit the government to move down the cost curve by using higher capacity, less expensive per bit lines (1.544 Mbps).

7.26 The penalty for failing to take action soon is likely to be a further balkanization of telecommunications facilities. Departments may continue to develop independent networks less able to benefit from future advances in technology and, therefore, further distance themselves from opportunities to gain from government-wide efficiencies.

7.27 Although the government obtains savings in voice communication expenditures through GTA, gradual reductions in the tariff rates for message toll and WATS services are eroding them. As this trend is likely to continue, and rates continue to decline for message toll services, GTA may be unable to maintain its overall economic viability.

7.28 The six departments included in this audit have all agreed in general with the conclusions reached, and with the potential for significant cost savings. They gave support to the concept of a government-wide focus to telecommunications and to the notion of a common service network. However, a caution was issued that any common service approach must ensure that it can maintain an adequate level of service to all users and satisfy the needs of departments requiring special consideration. We support these concerns.

GTA's mandate is unclear and has resulted in significant missed opportunities for efficiency gains

7.29 The reasons for GTA's unclear mandate became an important focus of the audit. We began by examining the roles and responsibilities of the organizations involved with telecommunications in the federal government.

7.30 The Treasury Board's Common Service policy designates GTA as the mandatory common service agency for the provision of telecommunications within the federal government. However, this is in conflict with the Telecommunications policy, under which departments can act on their own to obtain telecommunications services.

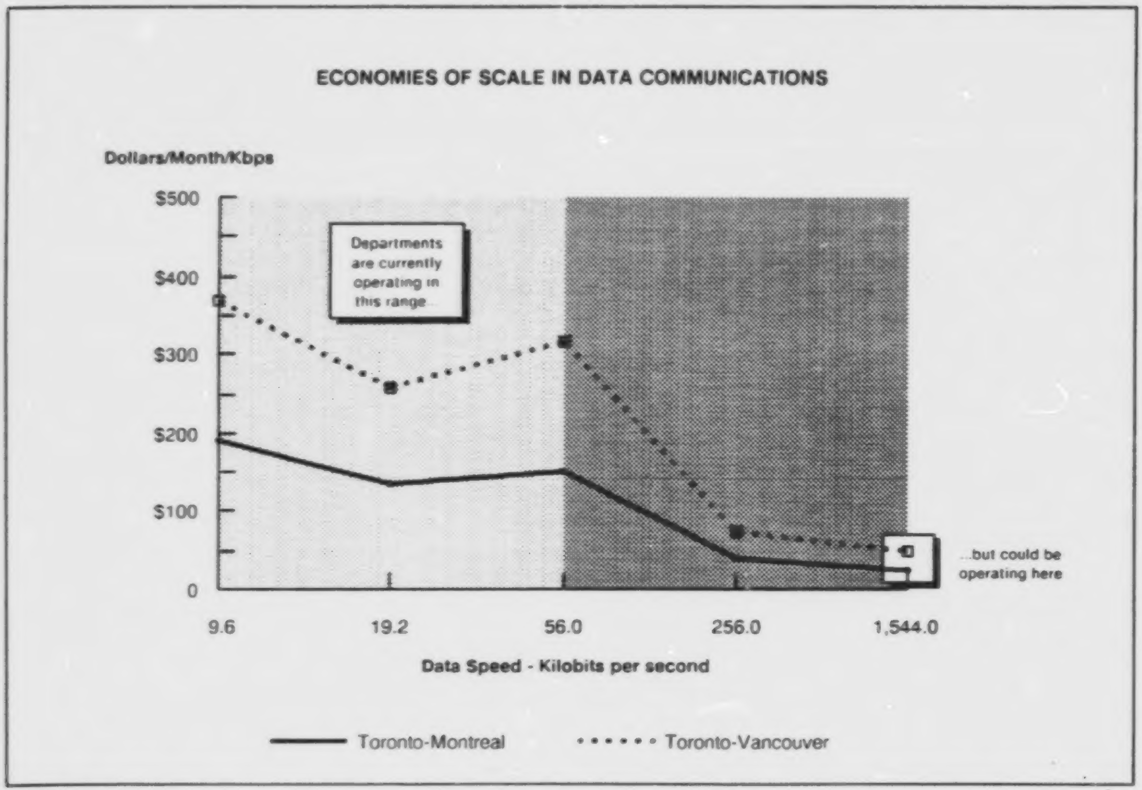

Exhibit 7.2

7.31 The Department of Communications, under Section 5(d) of the DOC Act, shall "...plan and co-ordinate telecommunications services for departments, boards and agencies of the Government of Canada." Within this legislation, GTA's mandate is " . . . to plan, establish and manage telecommunications facilities and services that will satisfy the requested needs of federal departments and agencies on an economic basis." This objective lacks the strong mandatory wording of the Treasury Board's Common Service policy. In addition, the Treasury Board does not enforce its mandatory common service policy for GTA. When reviewing submissions for telecommunication projects, we found examples of Treasury Board giving approval to projects before requiring that departments confer with GTA. For example, approved Treasury Board submissions from DPW and CEIC both stated that the departments should seek GTA's assistance, rather than enforcing the GTA role before approving the submission.

7.32 GTA has not established its administrative role for government data communication services. Inactivity on the part of the Treasury Board and DOC in establishing a co-ordinating body for data services has contributed to the lack of focus on administering government-wide data communications. The Treasury Board's current management philosophy, embodied by IMAA (Increased Ministerial Authority and Accountability), emphasizes that departments have increased responsibility to manage within their own scope of operations, with reduced intervention from central agencies. However, if the full potential of government-wide opportunities to improve efficiency is to be realized, it will require a central, co-ordinated focus. We believe that departments are not well placed to take full advantage of these opportunities without involvement from the central agencies.

We also noted a perception that IMAA discourages the government-wide co-ordination necessary to take advantage of telecommunications efficiency opportunities.

7.33 We found that conflicting authorities in the Treasury Board Common Service policy and Telecommunications policy have resulted in many departments planning and operating their own private data networks. Departments interpret the Treasury Board policy as giving them the option to lease common carrier packet switched data services rather than using the less expensive, GTA administered, GPN. Unless there are overriding security issues, the use of any service other than common service leads to inefficient telecommunications usage.

7.34 The Treasury Board established the Telecommunications Advisory Committee (TAC) to advise GTA on long-range planning and co-ordination of the use of telecommunications on a government-wide basis. The Advisory Committee on Information Management (ACIM), an interdepartmental advisory committee to the Treasury Board Secretariat, deals with the broader area of information technology. Neither these committees nor the Treasury Board appear to have a clear-cut position on whether a mandatory common service organization is required. This has contributed to the segmenting of government data traffic by departments and the development of networks which, collectively, result in higher costs. ACIM has recognized that the current data communications environment should be addressed and has tasked a sub-committee to report on telecommunications in the government.

With no clear leadership, the government is not positioned to take advantage of either the significant existing opportunities or the technological innovations that should soon be available.

7.35 The separation and lack of active co-ordination between TAC and ACIM also furthers the fragmented approach to telecommunications across the government. In most departments it is policy to regard telecommunications as two distinct services -- voice and data. Advances in technology are making this division less appropriate for the future.

7.36 The Treasury Board has no apparent mechanism for ensuring that departments treat telecommunications issues with a government-wide perspective. None of the parties -- Treasury Board ACIM, TAC, or GTA -- has shown any effective leadership in this area. As a result, the federal government is losing an opportunity for significant savings in the order of $30 million to $45 million a year at the present level of data communications expenditures.

Departments lack confidence in GTA's abilities

7.37 We noticed that user departments view GTA as simply a negotiator of bulk deals with the telephone companies. We believe that GTA's working relationship with departments has contributed to the perception that it cannot provide sophisticated data communications assistance and is mainly there for voice communication services. GTA is not positioned to exploit a dynamic technology for the greater efficiency of the government as a whole. For example, DPW has been unable to wait for GTA to identify and develop necessary services. DPW took action to provide a more efficient cabling system for its government buildings, to reduce costs.

7.38 There are several areas where co-ordination is needed to examine and evaluate the opportunities for government-wide savings. We believe action needs to be taken to enable departments, and the government as a whole, to plan for changes in technology and potential efficiencies in the following areas:

- new building cabling systems;

- assistance in understanding and remaining current on regulatory changes;

- in-depth data traffic analysis for the government as a whole;

- advice and leadership on the directions departments should take to be prepared for new service offerings such as Integrated Services Digital Network and voice-data integration planning; and

- telecommunications technology advances offered by the common carriers, and the application of these advances to government services.

7.39 The Treasury Board should:

- **ensure that an administrative infrastructure exists for all government telecommunications services, supported by a clear policy framework;**

- **ensure that this infrastructure supports a co-ordinating body, such as a common service agency, that has a government-wide perspective, responsibility, authority and capability to obtain or provide all telecommunications services for the departments and agencies of the federal government in an economical, efficient and effective manner; and**

- **ensure that the savings attainable with a government-wide approach to telecommunications administration are achieved through a co-ordinating body, and hold it accountable for realizing those savings.**

Management's response: *The Treasury Board Secretariat (TBS), and the members of the Advisory Committee on Information Management (ACIM), are well aware of these issues and have for some time been addressing them.*

In 1987, the Treasury Board approved and promulgated an Information Management Policy Overview entitled "Strategic Direction in Information Technology Management in the Government of Canada - 1987" which identifies these issues and other critical issues for the efficient use of Information Technology (IT) in the government. In 1988, the TBS promulgated, after endorsement by ACIM, a proposal for a new strategic planning process for the management and co-ordination of IT, with special emphasis on common service organizations and their planning role.

A proper planning base for IT across government is required if the potential dramatic savings and efficiencies are to be achieved. In close cooperation with ACIM, the TBS has proposed drastically new policy approaches to IT management, and incorporated the work of the various ACIM Working Groups. The proposals will be submitted shortly to Treasury Board, and implementation will start immediately after approval.

The Working Group of ACIM mentioned in the AG study, has been examining the situation for several months in some depth, and will soon table its report. Action will then be taken to put in place the necessary changes within the above mentioned new overall policy framework.

The TBS, as well as ACIM, see the problem as more complex than indicated by the AG study. The merging that is occurring is not only "voice" and "data", but also "telecommunications" and "computer systems". The government should therefore not only look to telecommunications carriers for solutions, but also to other suppliers. In this context, having a common service agency offering a "mandatory" telecommunications service, based almost solely on carrier offerings is not an adequate long-term solution. The Common Services Policy will be revised accordingly, in the light of developments in the use of IT and in the industry.

7.40 The Department of Communications should:

- **review the past performance and current capabilities of GTA to determine whether it is the appropriate vehicle for a common service agency for all government telecommunications;**
- **take action to clarify the mandate of GTA with respect to the intent of the Treasury Board's administrative policy framework; and**
- **re-examine the provision of common services for telecommunications, with a view to studying the role of a common service agency as re-seller of carrier services and negotiator of agreements similar to "master standing-offers" for services.**

Department's response: *The Department accepts the conclusions and recommendations of the audit and makes the following additional comments. Despite the very limited resources available, GTA has managed to implement common services for data communication in the forms of a VSAT network, a packet switched network and conversion of the circuit switched network of digital facilities, all of which have brought and will bring further economies to the government in the data communications area.*

It should be recognized that DOC does not have any power to enforce a common service agency role (implied mandatory) and, in the IMAA environment, such an action would be questionable. Short of the mandatory inference, the Department and GTA have vigorously pursued a common service role even to the extent of creating a marketing group to ensure the benefits of the common service approach are widely publicized throughout government.

The Agency has developed a plan (GTN 2000) which clearly shows the direction to achieve the greater savings which will become available in the future.

GTN 2000 examines the major changes in technology and regulation now unfolding and provides the blue print by which GTA will evolve a single universally accessible network to carry voice, data, image and video in the future. The baseline for this network is the existing circuit switched network which is being converted to a universal digital technology network as permitted by economy, technology and regulation. A Request for Information issued to industry in 1988 indicates that it will be feasible to establish a pilot digital channel network service by 1990.

8

FOLLOW-UP TO THE 1987 MANAGEMENT CATEGORY AUDIT

8

FOLLOW-UP TO THE 1987 MANAGEMENT CATEGORY AUDIT

Main Points

8.1 During our follow-up we noted improvements in policies and practices and, in some respects, significant differences -- both positive and negative -- in the attitudes and perceptions of members of the Management Category compared with 1987. For example, decisions regarding pay in 1987 and 1988, increased flexibility granted to deputy heads in relation to salary administration, semi-annual Assistant Deputy Minister updates, creation of the Canadian Centre for Management Development and visits to regions by heads of central agencies were seen by the Executive levels -- and to a lesser extent by the Senior Management level -- as positive and constructive (paragraphs 8.9 to 8.12, 8.46).

8.2 Although there have been improvements in practices such as job evaluation and staffing, many of the problems identified in 1987, notably in relation to the definition and composition of the Category, salary compression/inversion, human resource planning and career development and the accountability framework, continue to exist. In addition, pay for performance is still a major source of dissatisfaction. Efforts are being made to address elements of these issues. In some of the areas examined, the ability to make further progress is limited due to the existing legislation and thus depends on legislative change (8.13 to 8.89).

8.3 Departments, however, believe that they are still unduly constrained in the efficient and effective management of their management teams. Perceived constraints include the definition of "management personnel" and the lack of sufficient flexibility and delegated authority (8.19, 8.90 to 8.93).

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Exhibits

8.1 Distribution of Management Category Population by Level for 1986, 1987, 1988

8.2 Number of Vacant Positions Advertised by the Public Service Commission -- July 1988 - July 1989

FOLLOW-UP TO THE 1987 MANAGEMENT CATEGORY AUDIT

Introduction

8.4 Our 1987 audit of the Management Category examined policies, programs and practices related to the 4,300 members in the Executive (EX) and Senior Management (SM) groups in the federal public service at that time.

8.5 Our report contained observations and recommendations on the definition and composition of the Management Category, job evaluation, compensation and salary administration, performance management, resourcing, and the accountability framework for the management of programs related to the Category.

8.6 We found deficiencies that, taken as a whole, were working against key objectives in the creation of the Management Category such as the concept of an identifiable and cohesive managerial cadre.

Scope

8.7 In the follow-up we focussed on the changes that have taken place in Management Category policies and programs in the Treasury Board Secretariat, the Public Service Commission and the Privy Council Office since our audit, as well as changes in the practices in six departments.

8.8 Individual interviews and focus group discussions were conducted with EXs and SMs in the six departments to assess attitudes and perceptions of managers about Management Category policies, programs and practices.

Observations

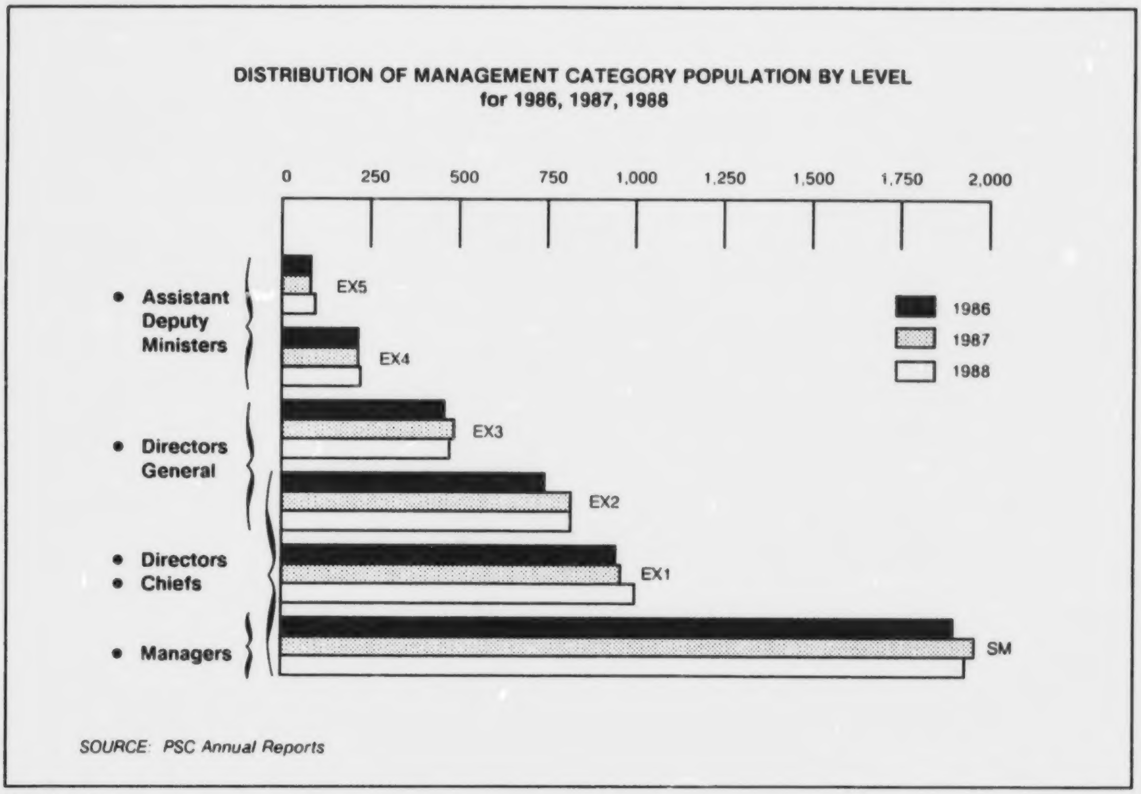
8.9 In conducting our follow-up we noted a number of initiatives undertaken since our 1987 audit which relate to the management of the Management Category.

Initiatives undertaken include projects on such things as values, internal communications, managerial attitudes, the creation of the Canadian Centre for Management Development and visits to regions by heads of central agencies.

8.10 Included are projects conducted under the direction or auspices of the Clerk of the Privy Council and the Committee of Senior Officials (COSO) and central agencies. These projects have focussed on such topics as values, managerial attitudes, the role of the public service manager and internal communications. Some of these projects have in turn contributed to other service-wide and departmental activities.

8.11 Other examples of initiatives are the creation of the Canadian Centre for Management Development, the institution of semi-annual Assistant Deputy Minister updates, the publication by the Treasury Board Secretariat of the Manager's Magazine and visits to regions by heads of central agencies.

8.12 Those interviewed, particularly at the senior levels of the Management Category, welcomed these initiatives.


DISTRIBUTION OF MANAGEMENT CATEGORY POPULATION BY LEVEL
for 1986, 1987, 1988

SOURCE: PSC Annual Reports

Exhibit 8.1

Definition and Composition of the Management Category: Progress, but Some Fundamental Issues Remain

8.13 Among the main deficiencies identified in 1987 was the lack of clear and consistent definitions of the Management Category and of "management personnel". This affected the degree to which people identified with the Category and management.

8.14 We found that, since the audit, and following a recommendation by the Advisory Group on Executive Compensation (AGEC), the Treasury Board Secretariat has returned (deconverted) 122 Management Category positions to their former occupational groups. This action has been greeted positively by some departments but with mixed feelings by others and by some of the individuals affected. It has alleviated some pay problems. These deconversions were the result of pressures from various sources, or of pay problems, rather than the result of a formal review of the concept and definition of the Management Category as recommended in our audit.

8.15 The Treasury Board Secretariat has undertaken a review of the close to 1,000 "Management Category Equivalent" positions -- positions with pay rates equivalent to or higher than those of many Management Category personnel -- to determine whether they should continue to exist as "equivalent" or be integrated into the Management Category. Some 50 percent of the incumbents are excluded from collective bargaining units and thus are eligible for consideration for inclusion in the Management Category. The Treasury Board Secretariat is also reviewing the "Management Category Complement", the control used to limit the number of Management Category and "equivalent" positions, in order to clarify its definition and simplify its administration. Workplans indicate a completion of these reviews in the fall of 1989.

8.16 The Treasury Board Secretariat has not formally addressed our 1987 recommendation to determine the extent to which the Management Category constitutes a service-wide and/or departmental resource. However, we found that, as noted in 1987, opinion is moving to a consensus that those at the Executive levels 4 and 5 constitute a service-wide resource. The Public Service Commission has created a Secretariat for a service-wide approach to planning for and staffing Executive level 4 and 5 positions -- Assistant Deputy Minister and equivalent. Although it is not a formal policy, Management Category personnel up to and including the EX 3 level are considered by departments as primarily a departmental resource.

8.17 Despite these changes, the Management Category continues to be composed of policy advisers, specialists and managers and to include only part of what most departments surveyed consider to be their management team. Some departments indicate that the Management Category represents less than one third of their "management personnel".

8.18 This situation persists because some of the fundamental issues identified in our 1987 audit still exist. For example, the Treasury Board Secretariat has not totally resolved the issue of which occupational groups should permit people to progress in their careers and salaries in parallel to those in the Management Category -- "dual streams". Furthermore, there is still a debate as to whether the concept of the Management Category should be extended to include some, or all, of the thousands of positions and individuals with managerial or supervisory responsibilities at the lower levels.

8.19 Some Treasury Board Secretariat officials and many of the departments surveyed still see the need for a better definition and identification of "management personnel". They believe that a certain number of individuals with significant management responsibilities should be excluded from collective bargaining and be clearly identified as part of management. They consider the current definition of "persons employed in a managerial capacity" -- for the purposes of the Public Service Staff Relations Act (PSSRA) -- as being too narrow, and the number of managerial exclusions from collective bargaining too few to ensure proper management representation, especially in field or regional offices. They are of the opinion that, as a result, they cannot create a strong sense of identity among their managers.

8.20 Despite announcements in January 1987 that the government was seeking a better definition of "persons employed in a managerial capacity", there has been no change so far. This issue was first raised in the 1974 Report on Employer-Employee Relations in the Public Service (the Finkelman Report).

8.21 Resolution of the managerial exclusion problem requires an amendment to the PSSRA. Exclusion from collective bargaining is the first criterion for consideration for inclusion in the Management Category; and it is also a first step toward a more clearly identifiable management team.

8.22 In reviewing the concept of the Management Category, consideration should be given to the fact that various surveys, including our own in 1987, have indicated that within the Management Category, as it currently exists, people at the SM level appear to have a different set of values and a different management culture than those at the EX levels. Their degree of satisfaction with the Management Category and some of its programs is much lower. There is a feeling of alienation, particularly but not exclusively in departments with scientific and professional populations. Some SMs believe they have been uprooted from the top of their former occupational group to find themselves at the bottom of a category in a group that has only one level. Their specialized qualifications, and the requirements of many positions, give them limited access to opportunities for advancement to the Executive level(s) or even lateral transfers.

8.23 Resolution of these issues regarding the definition and composition of the Management Category and of "management personnel" is necessary for the achievement of a strong and cohesive management team, both service-wide and at the departmental level. Furthermore, it could make it easier to control the number of management positions and to clarify access to mandatory management training, benefit entitlements and perquisites. More importantly, it would clearly identify those accountable for results.

8.24 The Treasury Board should review and clarify the definition and composition of the Management Category and of "management personnel" at the service-wide and departmental levels.

8.25 The Treasury Board should also review and reassess Management Category policies, programs and practices to ensure that they are consistent with the resulting definition.

Job Evaluation Practices: Improving Substantially

8.26 In our 1987 audit we observed that there was an inconsistent application of the Management Category Position (job) Evaluation Plan. Consistency is critical because job evaluation results are used in making salary comparisons with other sectors of the economy. Salary survey results are an important factor in determining compensation for the lower levels of the Management Category.

8.27 In 1987, job evaluation standards were incomplete; specialist training, management training and participation, resources devoted to job evaluation and information systems were inadequate; and there was no monitoring, review or audit.

8.28 These deficiencies made it inappropriate to delegate classification authority for Management Category positions, as intended at the time of the creation of the Management Category.

8.29 Substantial efforts and improvements have been made in job evaluation practices since our audit. Some of the initiatives undertaken by the Treasury Board Secretariat, however, had not been completed at the conclusion of our follow-up.

Benchmarks being reintroduced

8.30 The Treasury Board Secretariat is developing a new comprehensive set of benchmarks which it intends to introduce in the fall for use in the evaluation of Management Category positions. At present, the Secretariat is using "temporary" benchmarks. These have not been made available to departments; thus they are still without an essential element of the method used for evaluating Management Category positions.

Job evaluation specialists being trained

8.31 The Treasury Board Secretariat has taken measures to ensure that job evaluation specialists are trained in the use of the job evaluation plan for the Management Category. As of 1 July 1989, almost 150 job evaluation specialists had received training.

Still little management participation and training

8.32 The participation of managers in job evaluation is a fundamental principle of the Treasury Board's policy on job evaluation.

8.33 We found that there is still limited participation and training of managers in the job evaluation process for Management Category positions. In our opinion, the lack of management participation contributes to the continuing but unnecessary departmental practice of writing long, wordy job descriptions, which often are not sufficiently challenged. This weakens the credibility of the system. For example, there are managers in regions who think that the evaluation plan, and those doing the evaluating, do not always take into consideration all the complexities of their jobs compared with policy jobs and do not know the work as performed. Many managers admit, however, that they are not familiar with the system used.

8.34 In one of the six departments we examined, managers participate and have been trained in the Management Category job evaluation process. The reported result has been a better understanding of the relationship between organizational structures and jobs. There has also been a greater acceptance of, and satisfaction with, the job evaluation results.

Delays claimed to be reduced significantly, but high volume of classification activities

8.35 The Treasury Board Secretariat resource allocation problem observed in our 1987 audit has been partly resolved through reorganization. The service provided to departments is less reliant on transient expertise and, according to the Treasury Board Secretariat, delays reported in 1987 have been reduced by half. Controls are in place to ensure a steadier work flow and a faster turnaround time.

8.36 The Treasury Board Secretariat, however, indicated that the yearly volume of organization and classification activities for some 4,400 Management Category positions is between 1,500 and 2,000. According to experts, this is much higher than the volume that would be considered normal in the private sector and, in our opinion, it threatens the viability of the current approach to job evaluation. Furthermore, because of this high volume, evaluators cannot always devote enough time and attention to each job.

Information system: better, but could be further improved

8.37 The Treasury Board Secretariat has initiated projects to review and improve the system and the quality of information on Management Category job evaluation results. There have been improvements in the quality and accuracy of the data at the Treasury Board Secretariat level but the information has not yet been compared with that of departments, and the system in place does not yet permit the utilization of all the control features of the method used to evaluate Management Category positions. For example, we were informed that the system cannot produce an aggregate list of reporting relationships which would permit the monitoring of classification "creep" over time and the identification of opportunities for "delayering" -- that is, reducing the number of management levels. The Treasury Board Secretariat is taking steps to further improve the information systems and the quality of information.

Audit of job evaluation shows substantial improvements

8.38 The Treasury Board Secretariat has instituted a periodic audit of job evaluation activities and results.

8.39 The first audit report indicates a definite improvement in practices for jobs evaluated since our 1987 audit. Based on the sample of positions audited, it appears that the number of inconsistencies has been significantly reduced -- from over 40 percent in 1987 to 15 percent -- while 10 percent of the audited positions are possibly misclassified upward or downward. According to the consultants who carried out the audit, these results -- given the high volume of activity -- are as good as and possibly better than those found in private sector organizations using the same job evaluation system.

8.40 The Treasury Board Secretariat expects the consistency problem noted in our 1987 audit to be corrected over time, given the very high level of job evaluation activities for Management Category positions. However, the volume of job evaluation activity varies greatly from department to department and some jobs may not be reviewed for a long time. As there is no plan to ensure that all positions are reviewed over a reasonable, specified timeframe, the "health" of the system cannot be fully assessed. Because of the direct link between job evaluation results and the determination of Management Category pay, an assessment of the health of the system is critical.

8.41 The Treasury Board should continue its efforts to identify and address deficiencies in the Management Category job evaluation process and practices and, within a reasonable specified timeframe, ensure that all positions are reviewed.

8.42 It should consider, where appropriate and feasible, increased management participation and training in the job evaluation process.

Salary Administration and Compensation Practices: Less Salary Compression/Inversion, but the Issue not Entirely Solved

8.43 In 1987 we reported that salary compression/inversion was a prevalent problem in Management Category compensation.

8.44 Salary compression occurs when the salary range of a subordinate seriously overlaps the salary range of his or her superior. Salary inversion occurs when the maximum salary of a subordinate exceeds the maximum salary rate of his or her superior.

8.45 Salary compression/inversion was causing dissatisfaction and making it difficult to attract personnel to certain jobs either from lower ranks or from outside the public service. It had also resulted in ad hoc administrative practices such as salary protection and lump sum payments to keep pace with compensation of other occupational groups -- including collectively bargained groups.

8.46 The situation has improved since our 1987 audit. The Advisory Group on Executive Compensation in the Public Service (AGEC) made salary recommendations in 1987 and 1988, all of which have been accepted. In its June 1988 report, the AGEC stated that salary inversions had for the most part been resolved, and that salary compression had been brought under control. In addition, deputy heads now have some flexibility to determine salary on promotions, and in certain circumstances transfers.

8.47 Our follow-up in the six departments indicates that salary compression/inversion is not the major issue it was in 1987, particularly with the EX group. At the SM level, however, the salary compression/ inversion issue remains, though less acute than in 1987.

For example, some departments with SM positions with professional and scientific profiles are still experiencing salary compression/inversion problems.

8.48 In our opinion, salary compression/inversion situations continue to exist partly because the Treasury Board Secretariat has not addressed some of the issues identified in our 1987 audit.

8.49 In addition to the unresolved issue of determining who should be in the Management Category, there is the problem of the remaining inconsistencies in job evaluation results.

8.50 Furthermore, there is still no common basis for comparing compensation levels in the Management Category and those of other occupational groups, including collectively bargained groups -- with other sectors of the economy. As mentioned in 1987, there are fundamental differences in the methodology and process used for compensation surveys for the Management Category and, where available, those used for other occupational groups.

8.51 Unless the definition and composition of the Management Category is clarified and the level of inconsistencies in job evaluation results is brought down to a reasonable level service-wide, and until there is a common basis for comparing Management Category and other public service compensation with that paid in other sectors of the economy, the issue of salary compression/inversion is likely to recur. As stated in 1987, although it is important for Management Category compensation to pass the test of comparison with other sectors of the economy, it is equally important, if not more so, that internal relativity with other occupational groups be respected.

8.52 The Treasury Board should take further steps to improve relativity between Management Category compensation and that of senior levels of other occupational groups, and that of other sectors of the economy.

Performance Management Practices

Pay for performance: a major source of dissatisfaction

8.53 In our 1987 audit we reported that within the Management Category satisfaction was generally high with the performance appraisal process but that there was general dissatisfaction with "pay for performance".

Pay for performance practices continue to be a major source of dissatisfaction.

8.54 We found that the ceiling imposed on the total number of "Superior" and "Outstanding" performance ratings -- which are used in determining pay for performance -- and other aspects of the policy have created an even higher degree of frustration than in 1987.

8.55 The current Treasury Board pay for performance policy and its application by departments contributes to questionable practices. To varying degrees in the six departments surveyed there was evidence of the following:

- deciding on performance ratings without documenting or formally reviewing performance;
- documenting performance and deciding on a performance rating without input or discussion with the employee being evaluated;

- rotating "Superior" performance ratings among employees for reasons other than performance;
- granting two ratings: one used in determining pay (generally lower) and the other for performance assessment purposes;
- allocating a greater proportion of "Superior" ratings to the senior levels, thus limiting the possibility of recognizing or financially rewarding equivalent or better performance at the lower levels of the Management Category;
- as a departmental policy, refusing to consider or acknowledge "Superior" performance, whatever the performance, for people seconded to other organizations, or participating in task forces, etc., to give more to those who were with the department during the same period;
- failure or inability to recognize special or exemplary contributions of employees not rated "Superior" or "Outstanding".
- granting merit increases or bonuses without input from, or consultation with, the immediate superior of the employee being rewarded.

8.56 Another significant issue affecting the credibility of pay for performance is the perception that the policy and administrative guidelines do not adequately recognize, or provide sufficient flexibility to accommodate, the vast differences in the environment, philosophy, culture, nature of the work, management style and particular circumstances prevailing within departments.

8.57 The questionable practices and the perceived inadequacies of the policy have a detrimental effect on the credibility of the pay for performance program, notably among those at the lower levels of the Management Category.

8.58 Most of the six departments we surveyed believe it should be possible to develop pay for performance practices that are flexible and more compatible with their particular culture and environment. In that context, they see the Treasury Board Secretariat's role changed to creating a framework fostering better pay for performance practices rather than prescribing, controlling and administering. They believe these changes could greatly enhance the credibility of pay for performance.

More awareness of the importance of solving performance problems, but legislative constraints still exist

8.59 In 1987 we observed that performance problems in the Management Category were known but were not always appropriately addressed. There were certain practices that led to the transfer of responsibility for handling performance problems to other departments or central agencies like the Public Service Commission.

8.60 In our follow-up we found that, although the performance ratings "Satisfactory" and "Unsatisfactory" are still almost never used, in 1988 there was an increase in the overall utilization of "separation agreements", including financial incentives, as permitted under Treasury Board's separation policy for members of the Management Category whose performance is deemed not entirely satisfactory.

8.61 There is also a perception at the top levels of the Management Category that budgetary restraints, coupled with an increased sensitivity to this issue, are resulting in more attention being given to solving performance problems. This view is not always shared at the lowest levels of the Management Category.

8.62 We found, however, that "brokerage activity" on the part of the Public Service Commission -- i.e. the placement of Management Category personnel -- is as high as it was in 1987 and that the negative perceptions about the performance of some of the people on the "brokerage list" still prevail. This may be an indication that some transferring of responsibilities for handling performance problems is still going on.

8.63 The problems created by the existence of legislative constraints raised in our 1987 audit -- notably the multiplicity of legislative and other provisions each with its separate redress mechanisms, and the fact that only extreme cases can be dealt with under the current legislation -- have not been addressed.

8.64 The Treasury Board Secretariat informed us that it had initiated a review of the Management Category appraisal and pay for performance policies. At the conclusion of our follow-up, position papers and recommendations were being prepared for consideration by the Advisory Group on Executive Compensation (AGEC) and the Treasury Board Senior Advisory Committee (TBSAC).

8.65 In its review of the appraisal and pay for performance policies and guidelines, the Treasury Board should recognize:

- **the differences in nature and context among the different departments;**
- **the beneficial effects of involving departments in the design, development and implementation of more effective pay for performance practices and of improved ways to handle performance problems; as well as**
- **the need for flexibility.**

Resourcing Practices: Some Improvements but More Required

8.66 In 1987, we identified a number of deficiencies in resourcing practices -- staffing, human resource planning and career development and counselling activities -- for the Management Category.

Staffing: some positions being advertised, but more visibility and openness wanted

8.67 We observed in 1987 that staffing for Management Category positions was a relatively closed process, with limited or no information available on vacancies, processes used or resulting appointments.

8.68 In July 1988, the Public Service Commission published and distributed information on its staffing process for the Management Category, and began advertising within the public service some vacant Management Category positions. As of 31 July 1989 a total of 334 vacancies had been advertised. A significant proportion of these -- close to 60 percent -- were at the SM level (Exhibit 8.2). Most members of the Management Category interviewed were aware of these advertisements.

8.69 The Public Service Commission reports that advertising these vacancies has not unduly slowed the staffing process and that it has resulted in the identification of a number of good candidates and a number of appointments of individuals who would otherwise not have been considered.

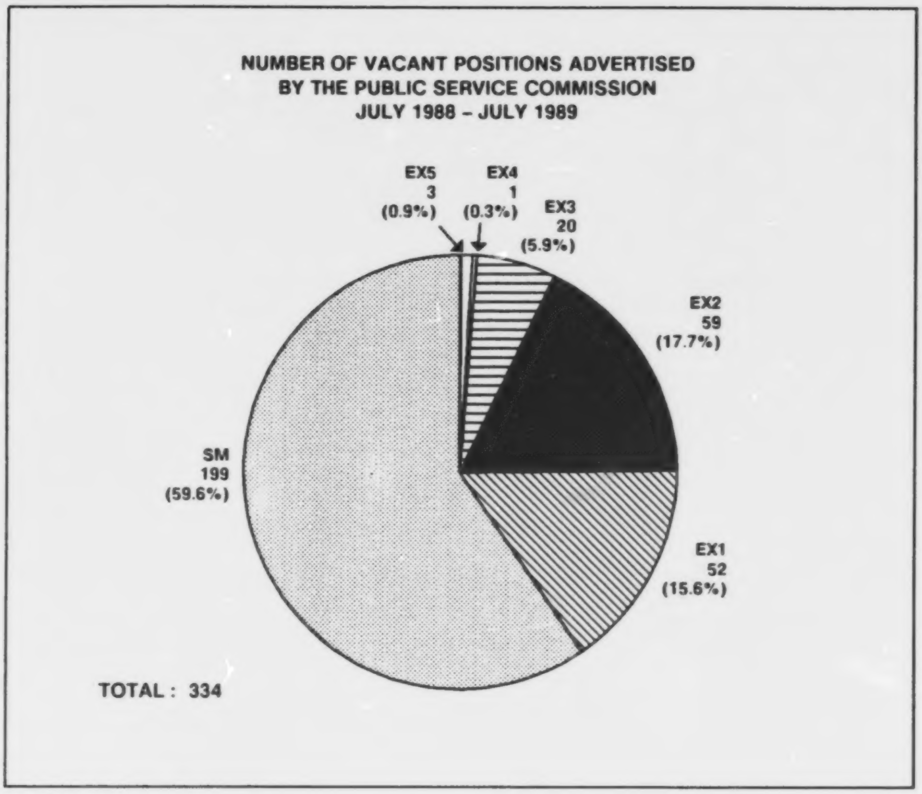


Exhibit 8.2

8.70 The Public Service Commission also publishes monthly, and distributes to departments, a list of its appointments. This information is not always adequately circulated by the departments.

8.71 Close to 35 percent of all Management Category appointments -- deployments -- are made by deputy heads under the Management Category Exclusion Approval Order (MCEAO). However, members still have little awareness of the openings, the process used, or the resulting appointments.

8.72 Persons interviewed in our follow-up perceived the Public Service Commission's advertising of some vacancies as a first step toward better understanding and increased visibility and openness of the staffing process. They did not, however, consider these efforts adequate to ensure a sufficient understanding of the processes used.

Human resource planning and career development: improvements required

8.73 In 1987 we observed that human resource planning and career development practices varied greatly among departments and involved mostly management at the Deputy Minister (DM) or Assistant Deputy Minister (ADM) levels, often with little or no input from individuals or even from their immediate superior(s).

8.74 The creation, in 1988, of a Secretariat in the Public Service Commission involved in the staffing of Executive level 4 and 5 positions (paragraph 8.16) has resulted in an increased service-wide sensitivity to the importance of developing people with DM potential, leading to improved career development practices for employees at those levels.

8.75 We have also found that the Public Service Commissioners are more directly involved in determining staffing strategies for Management Category positions that are staffed by the Commission's resourcing officers, to ensure that individual needs and public service plans and objectives are taken into consideration.

8.76 There was evidence of improved succession planning and of a greater awareness of the need for improved planning practices in some of the departments we surveyed. However, human resource planning and career development practices, where they exist, are still viewed with some skepticism. In some cases, they continue to involve mostly DMs and ADMs, and are focussed on "special interest groups" or on developing people with high potential. Many people interviewed during our follow-up were uninformed about the processes in place and even questioned the existence of such practices in their departments since they claimed not to be formally consulted or asked about their career plans or the potential of their subordinates for Management Category positions.

8.77 Public Service Commission data indicate that the average age of the Management Category population is rising faster than that of the rest of the public service. In the light of this fact, and of increased career plateauing and its potential effect on motivation, there is a need for substantial improvement in, and innovative approaches to, human resource planning and career development for all Management Category personnel.

More counselling, but regions still have limited access

8.78 In our 1987 audit we observed that Management Category personnel, notably those in the regions, had no, or very limited, access to Public Service Commission counselling.

8.79 The Public Service Commission reports that it has substantially increased the number of career counselling sessions it offers, although direct access in the regions is still limited.

8.80 The Treasury Board, the Public Service Commission and departments should improve resourcing practices to ensure that:

- **career interests and aspirations of members of the Management Category are, and are seen to be, considered in service-wide and departmental planning that addresses the requirements for an experienced and motivated managerial cadre;**
- **information is communicated and accessible on the various processes used and, where appropriate, additional opportunities are provided for input, participation and competition.**

Accountability for the Management Category

Roles and responsibilities more complex, but collaboration and co-operation have improved

8.81 In 1987 we reported that the accountability framework for managing the Management Category was weakened by the division of roles and responsibilities among central agencies and departments. Without a focal point, visible leadership and a forum for discussing and resolving problems, it was difficult to have an integrated approach to managing the Management Category and its programs.

8.82 Our 1987 recommendation on clarification of roles and responsibilities in relation to the Management Category and its programs has not been addressed by the Treasury Board.

8.83 Two major changes related to the roles and responsibilities for management of the Management Category and its programs have occurred since our 1987 audit.

8.84 The first change is the creation of the Canadian Centre for Management Development (CCMD), reporting to the Deputy Prime Minister.

8.85 The creation of the Centre has been seen by many as an indication of the government's commitment to improving management in the public service. Legislation which would clarify its mandate and accountability has been tabled in the House.

8.86 The second change is the increasingly visible leadership provided by the Clerk of the Privy Council -- whose role is not defined in legislation -- assisted by the Committee of Senior Officials (COSO), in managing the Management Category, and in initiating changes and influencing and co-ordinating the efforts of central agencies.

8.87 In our opinion, in the light of existing legislation and in the absence of a clear definition of "management personnel", roles, responsibilities and accountabilities for managing the Management Category and some of its programs are unclear.

8.88 Improved working relationships have permitted central agencies and departments to address some of the issues facing the Management Category. In our opinion, current working arrangements, however, do not provide the assurance, stability and continuity that a formal change in legislation would, nor do they permit exacting accountability for results. Because of the fragmentation of roles and responsibilities due to a complex legislative and administrative framework, an overall concerted strategy to address the concerns of both departments and members of the Management Category is much more difficult to develop, let alone implement.

8.89 Some people interviewed in the six departments surveyed have questioned whether the Public Service Commission can adequately protect the rights of individuals under the Public Service Employment Act (PSEA) and account to Parliament for the application of the Act to Management Category appointments while, at the same time, responding to management needs and being directly involved in human resource planning and career development initiatives.

Despite requests from departments for more authority, little progress

8.90 One of the objectives in creating the Management Category was to provide greater flexibility to Deputy Ministers to manage, deploy and develop their management teams. In 1987 we noted that the original plan to delegate classification had not been carried out. We also noted that the authority delegated to DMs to deploy has provided less flexibility than envisaged at the time of the creation of the Management Category, partly due to the "Management Category Complement" -- the control on the number and use of Management Category and "equivalent" positions.

8.91 Since the audit there has been some increase in the authority delegated to deputy heads for Management Category salary administration and other administrative matters, and increased flexibility in the use of the "Management Category Complement".

8.92 At the conclusion of our follow-up, despite departmental requests under the Increased Ministerial Authority and Accountability (IMAA) initiative, no additional authority for staffing and no significant authority for classifying Management Category positions had been granted to deputy heads.

8.93 There is a strong desire in some departments for more significant authority for the management of their managerial cadre within an improved accountability framework. There is also the perception that some Management Category programs, such as pay for performance, are over-administered but under-managed.

Monitoring, audit and accounting for results: little improvement

8.94 With the exception of the audit of job evaluation results instituted by the Treasury Board Secretariat, there have been no significant improvements in the monitoring, review, audit or accounting for results by central agencies and departments, for the use of delegated authority for the Management Category and its programs.

8.95 The government should ensure that the allocation of roles and responsibilities for the Management Category and its programs provides for:

- **a focal point for clear and visible leadership and direction;**
- **a planned and co-ordinated approach to providing to deputy heads the flexibility and authority necessary to manage their management teams efficiently and effectively; and**
- **improved accountability for results.**

9

INCENTIVE AWARD PLAN

9

INCENTIVE AWARD PLAN

Main Points

9.1 The government's Incentive Award Plan of six programs is intended to recognize the contribution public servants can make, with their imagination and performance, to the administration of the federal public service. We looked at two of the Plan's programs in six departments to see how they were working (paragraphs 9.13 to 9.15, 9.28 and 9.29).

9.2 Treasury Board Secretariat, responsible for the overall administration of the Plan, and departments and agencies with delegated authority to operate programs, all have roles to play. Those roles are not now being exercised in a way that will realize the Plan's full potential (9.12, 9.16 and 9.27).

9.3 Of the six programs in the Plan, two of them -- the Suggestion Award and Merit Award -- are designed to recognize that the ideas and efforts of employees can have both immediate and long-term benefits for the operation of the public service. These two programs are also important because of their influence by example on other public servants (9.17 to 9.22).

9.4 Only a limited number of departments participate in the two programs, and the number of participating employees is low (9.30 to 9.36).

9.5 There are exceptions, however. A number of organizations have active and successful programs. In these instances, senior management is visibly committed to the Plan and incentive programs to support it have been implemented that go beyond Treasury Board Secretariat policy requirements (9.37 to 9.40, 9.60 to 9.72).

9.6 There is no effective monitoring by Treasury Board Secretariat of Plan programs delegated to departments. Minimal resources have been allocated to the overall administration of the Plan, statistical data collected is of limited utility and the Plan has not been formally evaluated in the last ten years (9.45 to 9.51).

9.7 The Suggestion Award and Merit Award programs are not being used to their potential. This means the contribution that employees can make may not be fully recognized and utilized. It also means that opportunities to increase productivity may be overlooked and significant cost savings may be missed (9.52 to 9.54).

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INCENTIVE AWARD PLAN

Introduction

Perspective

9.8 Efficiency in government is a popular theme today where the focus is on systems, process, machines, and management involvement. All of these elements require, however, the intervention of public servants acting individually or in groups.

9.9 In the interests of greater productivity, public and private organizations today are striving to improve management and employee co-operation. There are many views on how this can be achieved, but no consensus on the "correct" view, no "right" approach.

9.10 However, it is generally accepted that a judicious blend of incentives will encourage employees to give their best.

9.11 Public service managers are aware of the part that rewards and recognition can play in reaching organizational performance goals. There is a sense that now is the time to improve the present system of employee involvement. Strong and supportive leadership is an indispensable part of this process.

9.12 In recent years, there has been considerable discussion about the decline in morale in the federal public service and its effect on the work environment. A potential exists for making some improvement to that environment through the Incentive Award Plan. It is well worth the effort required to do so.

9.13 It is the policy of the government to recognize significant contributions to the public service made by public servants. Employees are seen as valuable and knowledgeable sources of useful ideas and initiatives.

9.14 The Incentive Award Plan is designed to recognize these contributions.

9.15 Recognition is given for outstanding performance; for meritorious work contributions; for long service; and for submitting practical suggestions -- all having to do with making the federal government work better. The acknowledgment of these contributions is given by way of money or other means.

Incentive Award Plan

9.16 The Plan consists of six programs for which the Treasury Board Secretariat has overall responsibility. This includes the development of policy and procedures, basic program design, and monitoring and evaluation of the Plan's activities. To facilitate administration, the individual programs are separated into two categories of responsibility. One recognizes the needs of the corporate culture of the public service while the other acknowledges the need for autonomy on the part of the participating organizations.

Programs delegated to participating organizations

- Suggestion Award Program
- Merit Award Program

- Long Service Award Program

Corporate programs administered by the Treasury Board Secretariat

- Award of Excellence Program
- Outstanding Achievement Award Program
- Senior Officer Retirement Certificate Program

9.17 **Suggestion award program.** The Program's purpose is to recognize ideas from employees that will help improve and maintain productivity.

9.18 This program involves the largest number of eligible and participating employees and the most money spent.

9.19 The maximum amount that may be awarded for any one approved suggestion is $10,000, before taxes. According to statistics issued by Treasury Board Secretariat, for the fiscal years from 1986 to 1988, an average of $350 has been awarded to about 2,200 approved suggestions. For the same period, the average savings attributable to a suggestion have been $9,068 -- almost $26 saved for every dollar spent, plus, in some cases, other benefits that cannot be quantified.

9.20 **Merit award.** The Merit award is granted to those who have made significant contributions to the work of their organization or who have shown exceptional work performance.

9.21 This program may grant awards of between $500 and $3,000 to individuals and up to $6,000 to groups. Employees who are part of bonus or performance pay plans can receive only non-monetary recognition -- and then only up to a maximum value of $100. Under the Merit Award Program the average pre-tax award in 1987-88 was $520 to about 430 recipients.

We looked at how well two programs operating under the government's Incentive Award Plan were working.

9.22 These two programs are designed to include all members of the public service. Those in the management category may receive only non-monetary recognition.

9.23 The **Long Service Award** recognizes employees who have served 25 and 35 years in the public service.

9.24 **Award of excellence.** Started in 1986, this program represents a second layer of recognition. It is given to a small number of those who have already been recognized under either the Suggestion Award or the Merit Award Program.

9.25 The most meritorious recipients are invited to Ottawa, and in a special ceremony a minister of the government presents their awards. The objective is to give wider publicity to the contributions public servants are making to improve the economy and efficiency of government operations. One of the recipients of the 1989 awards was an employee of the Department of Supply and Services who saved over $12 million by negotiating reduced charges from United States government agencies.

9.26 The names of the final two programs describe the basic criteria that apply to them. The **Outstanding Achievement Award** is directed at management category public servants for distinguished service and accomplishments in the course of their careers. The

Exhibit 9.1

SUGGESTION AWARD PROGRAM
1987-1988

Organization	Number of Employees	Suggestions Received	Suggestions per 100 employee	Number of Awards	Value of Awards	Average Award	Value of Savings	Average Savings
Agriculture Canada	13,113	63	0.48	10	$ 8,245	$ 825	$ 203,285	$20,328
Canada Labour Relations Board	103	0	0.00	0	0	0	0	0
Canadian Human Rights Commission	176	1	0.58	0	0	0	0	0
Canadian Transport Commission	672	0	0.00	2	1,033	517	14,035	7,017
Communications Canada	3,052	18	0.60	8	900	133	2,542	318
Consumer and Corporate Affairs Canada	2,265	27	1.22	8	1,913	239	16,024	2,003
Employment and Immigration Canada	28,512	905	3.24	175	46,737	267	1,364,270	7,796
Energy, Mines and Resources Canada	5,232	34	0.66	19	8,251	434	121,528	6,396
Environment Canada	10,366	106	1.04	21	9,704	462	234,089	11,147
External Affairs	8,621	16	0.19	1	875	875	26,923	26,923
Finance, Treasury Board, Comptroller General	1,674	16	0.97	0	0	0	0	0
Fisheries and Oceans	6,131	28	0.47	7	2,185	312	10,752	1,536
Health and Welfare Canada	10,000	29	0.30	0	0	0	0	0
Indian and Northern Affairs Canada	4,902	4	0.08	1	300	300	1,000	1,000
Justice Canada	1,684	1	0.06	1	1,000	1,000	3,000	3,000
Labour Canada	900	2	0.23	0	0	0	0	0
Library of Parliament	239	10	4.27	4	300	75	0	0
National Archives of Canada	784	3	0.39	1	1,485	1,485	32,757	32,757
National Defence	120,311	532	0.45	212	99,700	470	2,649,799	12,499
National Energy Board	358	2	0.55	0	0	0	0	0
National Library of Canada	560	5	0.91	1	400	400	0	0
Public Service Commission of Canada	2,450	21	0.87	4	2,165	541	16,153	4,038
Public Works Canada	8,000	54	0.69	17	5,194	306	95,941	5,644
Regional Industrial Expansion	2,600	6	0.24	0	0	0	0	0
Revenue Canada (Customs & Excise)	10,482	232	2.26	17	9,610	565	301,911	17,759
Revenue Canada (Taxation)	18,000	553	3.13	48	11,775	245	294,029	6,126
Royal Canadian Mounted Police	20,042	128	0.65	7	2,515	359	15,597	2,228
Secretary of State	3,001	15	0.51	1	50	50	0	0
Statistics Canada	4,818	42	0.89	9	2,455	273	20,340	2,260
Supply and Services Canada	9,989	176	1.80	54	20,455	379	745,221	13,800
Transport Canada	19,805	410	2.11	245	67,344	275	1,068,045	4,359
Veterans Affairs Canada	4,350	57	1.34	16	4,465	279	6,705	419
	323,192	*3,496*	*1.10*	*889*	*$ 309,056*	*$ 348*	*$ 7,243,946*	*$ 8,148*

SOURCE: Treasury Board Secretariat

MERIT AWARD PROGRAM STATEMENT OF OPERATIONS
1987 - 1988

Department	Number of Recipients	Value of Non-monetary Awards	Value of Cash Awards
Agriculture	5	$ -	$ 9,500
Consumer and Corporate Affairs Canada	20	-	19,000
Employment and Immigration Canada	76	1,600	37,046
Energy, Mines and Resources Canada	46	-	23,500
Environment Canada	26	900	10,500
Finance, Treasury Board, Comptroller General	122	2,365	33,615
Fisheries and Oceans	33	500	18,500
Indian and Northern Affairs Canada	2	100	300
Justice Canada	4	90	3,000
Labour Canada	1	100	-
National Defence	23	-	25,500
National Energy Board	6	-	3,000
Regional Industrial Expansion	4	-	1,500
Secretary of State	2	-	2,000
Statistics Canada	11	-	8,600
Supply and Services Canada	22	-	8,000
Transport Canada	18	-	13,600
National Capital Commission	11	-	1,080
TOTALS	**432**	**$ 5,655**	**$ 218,241**

Source: *Treasury Board Secretariat*

Exhibit 9.2

Senior Officer Retirement Certificate is presented by the Governor General in a public ceremony to retired public service executives of senior rank.

9.27 Deputy heads of participating organizations have been delegated responsibility for funding and administering positive and effective programs. They are expected to seek the participation of their employees in improving government operations. Ministers are also called on to support the program. Senior managers are expected to support the program visibly, not only by participating in award ceremonies but also by issuing periodic policy statements.

Scope

9.28 This audit examined how Treasury Board Secretariat administered the Incentive Award Plan and how participating organizations executed their delegated responsibilities for some individual program components. We also sought to understand why some departments were participating more actively than others in the full range of programs the Plan offers.

9.29 We focussed on the two main programs delegated to departments, the Suggestion Award and the Merit Award.

The President of the Treasury Board presenting a 1989 Award of Excellence to a public servant who saved the government over $12 million (see paragraph 9.25).

Findings

Low participation rate may be resulting in lost opportunities for cost savings

9.30 The rate of participation in the Suggestion and Merit Award programs by organizations and by employees is low.

9.31 Only 34 of approximately 140 eligible departments and agencies participated in the Suggestion Award program in 1987-88. (In practical terms, the Treasury Board Secretariat has contact with about 50 departments and agencies.) Their employees participated at a rate of 1.1 suggestion for every 100 employees. Over the past five years the rate has averaged almost 0.9 percent.

9.32 The National Association of Suggestion Systems, an organization supporting employee involvement programs, publishes annual statistics of its members' activities, in both public and private sector North American organizations.

Opportunities for improved productivity and significant cost savings are probably being missed.

9.33 The Association reported that in 1987, in the United States federal government, 3.9 suggestions were submitted for every 100 employees. The same report noted that other governments, some in Canada, reported an average of 1.0 submission for every 100 employees. North American employment sectors reported these rates per 100 employees:

Finance and business	13
Insurance companies	17
Consumer goods	14
Public transportation	5

Compared to these organizations, the public service is being tapped for fewer potential suggestions for improving efficiency. While the organizations with which this comparison is made are not exactly the same as the public service, they have similar administrative and paper burden workloads associated with large organizations.

9.34 Participation was also low in the **Merit Award Program**. In 1986-87 and 1987-88, 17 and 18 departments and agencies respectively, out of about 50, used the program or parts of it. Of the six departments we examined, four had given the award in the past two years, involving 317 employees and about $170,000 in awards.

9.35 In other words, little use is made of one of the two ways available to monetarily and directly reward employees and managers.

9.36 The reasons for the low participation rates cannot be determined precisely. Limited resources at the corporate as well as the departmental level may be one reason. Treasury Board Secretariat devotes two persons and modest funds to the overall program while departments dispense varying resources to this area. This leads to a number of questions regarding the management of a program that has not been formally evaluated in over 10 years, such as:

- are the rewards sufficient?
- is senior management committed?
- is there too much red tape?

Another reason may be insufficient marketing of the programs to senior management. Whatever the reasons, it is apparent that potential benefits to the organizations and to the employees are probably being lost.

Some programs working well, others not

9.37 There is a wide variety of practices used to implement incentive awards in the six departments examined, ranging from innovative, successful programs in some organizations to limited activity in others.

9.38 Organizations with active and successful programs have usually linked them to a philosophy of management that emphasizes the importance of people. They have had strong support from their Deputy Ministers, who have been actively involved in the programs. In addition, these organizations have taken other incentive initiatives that go beyond the original policy. Participation rates are higher.

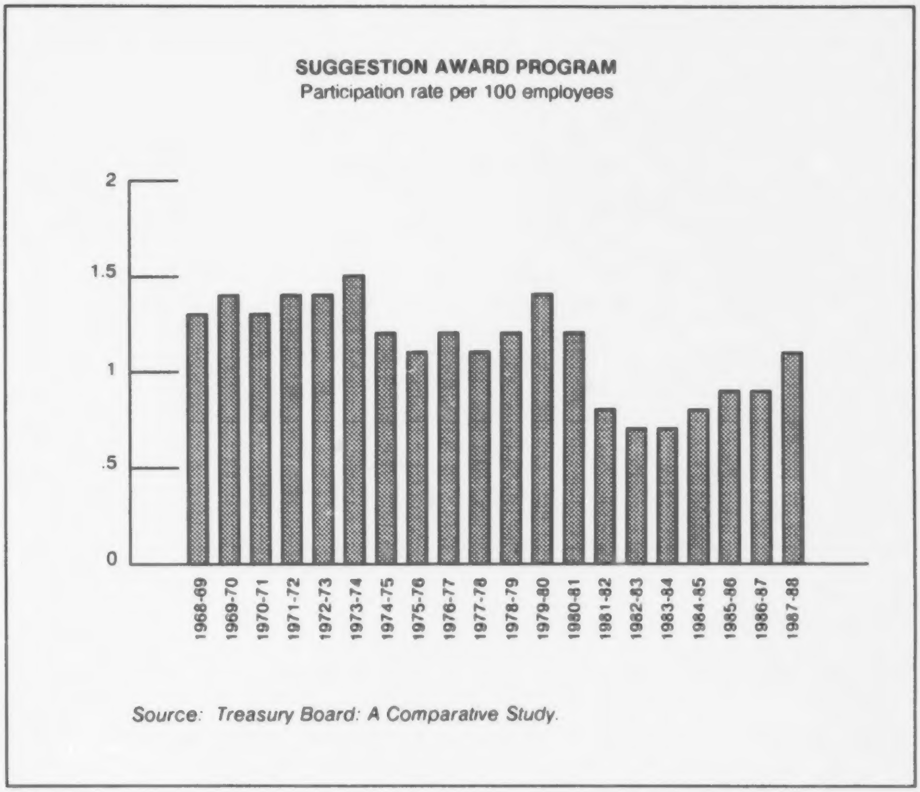
9.39 In March 1989 the Canadian Centre for Management Development published a paper, "A Management Model," a consensual review of management from the viewpoint of a Deputy Minister. Of the seven elements deemed essential to successful management four involved people. The four elements were:

- leadership,
- motivated, competent and productive staff,
- innovation, and
- effective internal communications.

These same elements play a part in the Incentive Award Plan, particularly the Suggestion Award and Merit Award programs. The Suggestion Award program, for example, is about innovation, communications and productivity and invites supportive leadership.

9.40 An example of leadership is Employment and Immigration Canada, which has a dynamic incentive award program in place. Some of its chief features are worth noting to understand why the program is more successful than others (see paragraphs 9.60 to 9.72).

Participation rate has not changed significantly over the years.



SUGGESTION AWARD PROGRAM
Participation rate per 100 employees

Source: Treasury Board: A Comparative Study.

Exhibit 9.3

9.41 Departments and agencies where activity was low were often operating with fewer resources applied to the program. To our mind, the level of resources appeared to be a measure of the support given to the program by senior management. However, employees and managers even in departments with low activity recognized the importance of incentive programs directed at their employees.

9.42 One reason advanced for lack of interest in the Suggestion Award program was the low financial reward. The financial awards are not high and they are taxed, so the net effect in most cases is not significant. The factor of "recognition," however, should not be lightly dismissed.

9.43 Departmental co-ordinators, on whom much of the immediate responsibility for the administration of the program rests, are carrying out their duties diligently given the time and resource constraints and the degree of management support provided. We noted no major deficiencies in compliance with policy. All organizations examined had adequate file systems where files were current, complete, and provided for follow-up as necessary.

9.44 However, we found that most organizations could not analyze results of their programs by region, organization, employee level, type of suggestion, etc., or establish track record profiles of any kind. Thus, data valuable to the management of the programs were not available. Annual reports are generally prepared for management, containing the information required by Treasury Board Secretariat. No other analysis is usually prepared.

Treasury Board Secretariat involvement ineffective in departmental programs

9.45 The Treasury Board Secretariat is devoting minimal resources to the Incentive Award Plan. There is no effective monitoring or evaluation of departmental programs and statistical information is limited.

9.46 As a reflection of the policies of decentralization and restraint, resources in the Secretariat are limited to two person years and a direct operating budget of $119,000 for 1988-89. This is down from five person-years in 1984-85.

9.47 The Secretariat is advised by the Incentive Award Board, a committee of senior departmental and central agency managers, which also acts as a forum for the discussion of problems. The Secretariat is frequently telephoned for help with departmental questions arising from the Plan and, by way of promoting the Plan and employee achievements, it has distributed two video productions throughout the Public Service. Finally, the Secretariat has recently received two awards for its promotional materials.

9.48 However, there are some deficiencies in the co-ordinating role and perhaps in the support role played by Treasury Board Secretariat. For example, no courses are available to departmental co-ordinators or managers. Also, the role of the Secretariat is perceived by staff of the departments we examined to be weak and of limited help. We were also told that:

- Treasury Board Secretariat is not working as a facilitator or networker though the policy suggests that it should. It is not communicating information and data to departments, or pursuing the clarification of policy and simplification of manuals.
- There is no formal and automatic mechanism for passing a valuable suggestion on to other government departments that might be interested in using the idea or adapting it to suit their purposes, although the policy suggests that deputy heads have this responsibility.
- Promotional material received from Treasury Board Secretariat is considered to be of low quality and not persuasive.

These somewhat mixed signals -- reasonable arrangements at the centre with problems felt at the periphery -- suggest some need for improved communications within departments and between departments and the Secretariat.

9.49 Treasury Board Secretariat needs to take advantage of the courses and meetings offered by the National Association of Suggestion Systems, of which the Government of Canada is a member. Some departmental co-ordinators have attended such meetings.

9.50 Statistical data that would illuminate aspects of the programs, particularly the Suggestion Award program, is limited. Data are collected to provide the Secretariat with the overview statistics it requires; data telling something about the origin of the suggestion, the organizational unit involved and its geographical location, the employee category and level, and details on the substance of the suggestion are not available. Such data would be useful in planning and marketing the award programs. Furthermore, generic government problems and solutions could be identified.

9.51 Treasury Board Secretariat is required to periodically monitor and evaluate the Incentive Award Plan, the effectiveness of its terms and conditions, and compliance with its rules. No formal evaluation has been conducted in the past 10 years.

Conclusions

What can be done to make it work better?

9.52 The existence of an underutilized suggestion and merit award system in the federal government, particularly as it affects the non-management categories of employees, means that employee participation and grass-roots identification of performance improvements may be lost. It further means that the skills of employees may not be fully used and, thus, their efforts are not being sufficiently recognized. The loss of opportunities to recognize employee efforts may contribute along with other factors to an undermining of morale and of a sense of personal involvement, satisfaction, and job commitment.

9.53 Opportunities to achieve greater productivity may be overlooked and significant cost savings are probably being missed. In the Suggestion Award program, for example, assuming that approved suggestions and gross savings would increase in proportion to any increase in the number of suggestions received, and bearing in mind the present low level of activity, doubling the number of suggestions (from the current figure of 1.1 per 100 employees in the 34 participating departments and agencies), would double the potential gross savings to approximately $14.5 million. If the overall ratio were to match Employment and Immigration's 3.2 per hundred employees, the gross savings could increase to $21 million. Most of these savings would continue year after year.

9.54 Although only 34 organizations actively participate, there are about 140 within the public service that could benefit from the program. This is one measure of the size of the opportunity.

9.55 During our audit there was strong recognition on the part of many managers and employees that much more needs to be done in the area of employee rewards and recognition -- that tangible and intangible benefits would be significant and that employees need to be encouraged to contribute their ideas. Reward and recognition programs initiated by management can play a part.

9.56 Other representatives claimed that achieving the ideal of free and easy movement of ideas in hierarchical organizations is probably impossible. Employees are naturally cautious about advancing ideas that may appear to question management's implicit approval of the way things are presently done. Nonetheless, attitudes towards the program were generally positive. Many felt that an incentive plan, alive and well, demonstrated a healthy corporate culture.

9.57 There are no easy answers for making the Plan, or its individual programs, work better. But we offer the following recommendations in the belief that their implementation would aid in encouraging greater participation and visibility that would help free the creativity and enthusiasm of public servants.

9.58 Treasury Board Secretariat should:

- **develop methods to regularly remind all deputy heads and senior management about the range of employee involvement tools available through the Incentive Award Plan and of the necessity of employee participation in identifying productivity improvements.**

- **encourage more experimentation in incentive programs. In fact, many of the departments we examined had developed some of their own incentive programs with Treasury Board Secretariat assistance.**

- **determine what statistics are needed to identify the sources of suggestions, the active occupational groups, and the subjects where improvements are being suggested. The Secretariat should consider establishing a shared computerized data base for that purpose.**

- **examine whether the present monetary award arrangements can be improved.**

- **examine whether less traditional rewards may be used.**

- **try networking and other procedures to ensure that valuable, cost-efficient and productive ideas are brought to the attention of other departments for their possible use.**

- **develop stronger links with the departmental co-ordinators and upgrade the quantity and quality of their training programs, which should involve managers.**

9.59 Departments and other participating organizations should:

- **make rewards and recognition a management priority.**

- **commit resources corresponding to the priority given.**

- **ensure that managers and co-ordinators participate in training sessions.**

- **develop suitable promotional campaigns in support of the programs.**

Example

A plan that works - Employment and Immigration Canada

9.60 Breakthroughs and originality. The Department of Employment and Immigration is an example of a department where the Incentive Award Plan is linked to a broader philosophy of management that encourages employee recognition and rewards as an ongoing management practice and as part of the organization's culture.

9.61 The Department has been exploring ways to create a healthier, more efficient organization while maintaining high-quality service. In 1986 it announced a "Philosophy of Management", the outcome of management workshops that had taken place across Canada. This philosophy is the cornerstone on which the Department is now managed. It emphasizes that people are the organization's most valued resource, a philosophy to which senior management has committed itself.

9.62 In 1987, the Department established three task forces to give effect to this philosophy. One task force dealt with recognition and rewards. The results of its work were published by the Department and made available to all employees. The current Incentive Award initiatives in the Department are an outcome of this work.

9.63 A foundation well laid. The departmental incentive award programs are based on three principles:

- A committment by senior management to visibly support the recognition and reward program.

- Good management practices to ensure that every employee is fully valued and treated with respect.

- Credit given to managers for using the Plan to recognize and reward excellence.

9.64 Active suggestion award. The Department has an active suggestion award program for soliciting and recognizing innovative ideas to improve departmental programs. The Department's level of participation is among the highest in the federal government. Of the 34 organizations reporting in 1986-87, Employment and Immigration Commission stood first among large departments in the percentage of participating employees and the cash awards given by the program. For every 100 employees, 3.1 suggestions were submitted, compared to an average of less than one in all the other participating departments.

9.65 Reaching out to regions. In some departments suggestions are evaluated only at Headquarters. In Employment and Immigration, regional review committees evaluate and approve suggestions that are specific to the region. This helps to assure a link between the management process and all employees.

9.66 Merit awards used flexibly. In 1988-89 Employment and Immigration awarded 89 merit awards. Of these, 57 were certificates and non-monetary awards up to a value of $100; the remaining 32 were certificates, cash, and merit award pins to recognize exceptional performance. With the concurrence of Treasury Board Secretariat, the authority to approve monetary awards up to $1,000 has been delegated to the regional and national headquarters group levels and the authority to approve non-monetary merit awards valued up to $100 has been delegated to the local level on a trial basis. This allows managers at all levels to become involved, as well as encouraging the frequent and timely recognition of smaller but genuine accomplishments.

9.67 Teamwork deserves recognition too - outstanding team award. In 1988, the Department initiated an award to the outstanding teams in Canada Employment and Immigration Centres, as well as at Regional and National Headquarters, with a one-time allocation of $15,000 for operations and maintenance expenditure. Through a self-nominating process, teams who felt they met the selection criteria were reviewed by a national selection committee consisting of a panel of eleven regional managers and one member from outside the Department. The participation of all members of all teams that applied was recognized and the Deputy Minister personally made the presentations at the winning teams' worksites.

Those incentive programs that are successful have strong Deputy Minister support.

9.68 Long service pin. Besides the regular plaques and medallions granted for long service, the Department also issues an Employment and Immigration pin. The Department is currently exploring further rewards for employees with significant length of service.

9.69 Exploring other possible ways. In addition to these formal programs, senior management has been encouraged to meet with employees to discuss reward and recognition initiatives specific to the values that teams recognize as being important in their own areas of work. In Employment and Immigration, managers are held to account for their activities in this area when their performance is appraised.

9.70 Sometimes a thank you goes a long way. The formal programs are viewed as only part of much broader set of management practices that encourage ongoing recognition and rewards. The Department recently completed an evaluation which showed that there are many practices in place to recognize employee contributions, including non-monetary rewards. Some managers have found that employees appreciate something as simple as a "thank-you" note as a token of recognition for extra effort.

An employee of Employment and Immigration being presented with a merit award in recognition of 45 years of reliability and dedication (see paragraph 9.66).

9.71 Publicity gets attention. These programs have high visibility in the Department. In addition to providing a related handbook, the Department has used a number of channels to communicate with employees, including desk drops, mailers with paychecks or direct deposit statements, posters, newsletters, videos and repeated reminders from senior management expressing its support for the programs. The Department is planning an ongoing awareness day to give more visibility to these programs.

9.72 Bringing it together. Employment and Immigration has made a concerted effort to create a culture that fosters awareness of the value of people in the workplace. The senior management team has acknowledged that one critical element in creating this environment is the recognition given to employees for their contributions to the goals of the organization. The practices that are currently in place demonstrate that the Department has made considerable progress toward these goals.

10

ELECTIONS CANADA

10

ELECTIONS CANADA

Main Points

10.1 The *Charter of Rights and Freedoms* declares that:

> *"Every citizen of Canada has the right to vote in an election of members of the House of Commons or of a legislative assembly and be qualified for membership therein."*

10.2 Federally, the Canada Elections Act gives effect to that right by organizing a major administrative part of the federal electoral machinery through the Chief Electoral Officer, a central player in our parliamentary democracy (paragraphs 10.9 to 10.12).

10.3 The efficiency and economy of the operations of Elections Canada are tied closely to the legislation that governs it. In recent years the Chief Electoral Officer has drawn Parliament's attention to problems besetting the Canada Elections Act and the electoral machinery. However, changes in our electoral legislation needed to deal with these problems and to maintain an electoral system of a quality respected throughout the world have not been made (10.15 to 10.26).

10.4 Over the years Elections Canada, under the direction of the Chief Electoral Officer, has sought to provide Canadians with an effective electoral service. However, the continuing effectiveness of that machinery is at risk. A number of factors are making it more difficult to guarantee an electoral service of the quality Canadians have grown accustomed to (10.15 to 10.26).

10.5 Some of the requirements for change arise from social changes in Canada such as the significant number of Canadians who travel or live abroad, the difficulty of enumerating an increasingly mobile and urban population, and the introduction of the *Charter of Rights and Freedoms* (10.27).

10.6 The outdated legislation has also led to inefficient procedures and high cost in administering the electoral process (10.28 to 10.36).

10.7 Preoccupied with these problems, Elections Canada has also not given adequate attention to analysis, planning, financial management, and internal organizational matters. This has further impaired its efficiency and economy and is bound to have an impact on its effectiveness (10.55 to 10.103).

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ELECTIONS CANADA

Introduction

10.8 The *Charter of Rights and Freedoms* declares that:

> *"Every citizen of Canada has the right to vote in an election of members of the House of Commons or of a legislative assembly and be qualified for membership therein."*

10.9 Maintaining a well functioning electoral machinery is not inexpensive: the 1988 federal general election should probably cost about $100 million with another $20 million to be spent on the reimbursement of party and candidate expenses.

10.10 Elections Canada, under the Chief Electoral Officer, is responsible for administering the federal election process and machinery. It is a small organization -- slightly over 50 full-time public servants based in Ottawa. In 1988-89 its direct operating costs were $2.5 million, of which over 85 percent was for salaries.

10.11 In planning for and administering elections, the staff of Elections Canada dispense election supplies, training, administrative services and advice to election officials across Canada before, during, and after each election.

10.12 Much the larger part of the organized electoral machinery originates with the returning officer -- one officer for each of the 295 federal electoral districts. That machinery springs to life only when an election is called and involves over 200,000 election officials. As one Canadian political scientist put it, "The modern electoral system is a loose-limbed colossus which lies dormant most of the time."

Audit Scope

10.13 We looked at Elections Canada's major activities in support of the electoral machine. Our audit also covered the administrative features of the Canada Elections Act and their effect on the operations of Elections Canada.

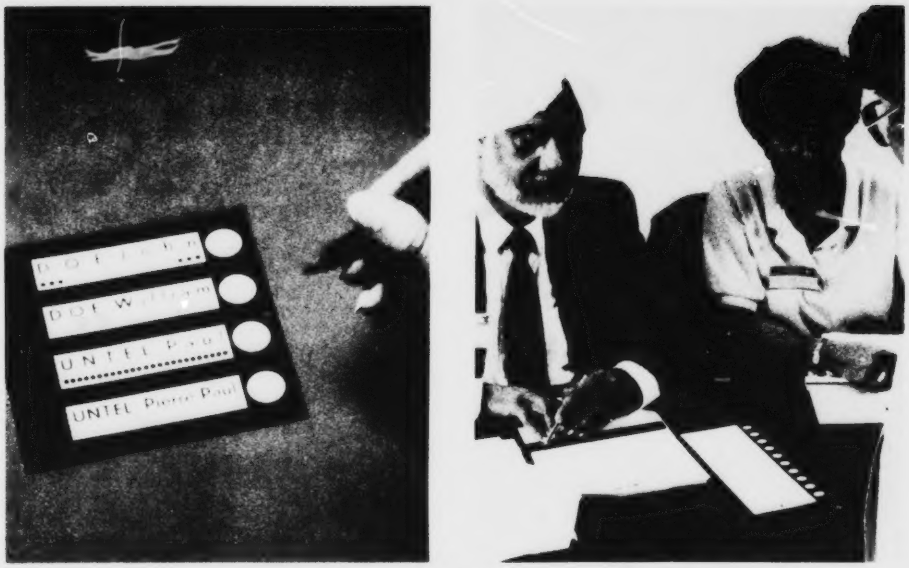
10.14 We did not look at the role of the Commissioner of Canada Elections, which had recently come under the scrutiny of the Standing Committee on Elections, Privileges and Private Members' Business; electoral work undertaken by Elections Canada in support of the *Electoral Boundaries Readjustment Act* and election expenses of parties and candidates, which will be examined in subsequent audits; or the work by Elections Canada on behalf of the Northwest Territories, which appears to have reached an end since the Territories plans to appoint its own Chief Electoral Officer for its next territorial election.

The Electoral Process

A complex operation involving time, people and geography

10.15 Although the act of marking a ballot is a simple task for the voter, it is but one visible step in an electoral operation largely obscured from view, where many administrative tasks have to be co-ordinated to support the voting process (see photo).

13.5 million persons voted in the 1988 election out of an electoral population of 17.6 million (see paragraphs 10.15 and 10.16).



Tip of the iceberg: marking the ballot -- one small part of the electoral process.

10.16 Canadians turn out in large numbers for their federal general elections: for the past two elections about 75 percent of the electors listed. In 1988, some 17,600,000 persons were eligible to vote.

10.17 The minimum federal election period is 50 days and recent general elections have averaged near that. More than 200,000 election officials are involved, many of whom are nominated by official candidates and political parties. Approximately 600 tons of supplies are shipped from Ottawa to constituencies across the country.

Shared responsibility among Elections Canada, government, and political representatives

10.18 Although Elections Canada is the administrator of the electoral machinery, it is not the undisputed manager. Under the procedural provisions of the Canada Elections Act, responsibility for the management of the electoral machinery is shared among Elections Canada, the government, and the political parties represented in the House of Commons. Each must co-operate with the others to achieve the intent of a smoothly functioning electoral machine.

We looked at how Elections Canada managed its operations and administered its responsibilities under the Canada Elections Act.

10.19 The government of the day is one of the managers because it is empowered by the Canada Elections Act to appoint new returning officers. In this appointment process Elections Canada has no influence and must rely on the government to appoint returning officers of adequate quality with whom it will work. The government also controls the number of full-time employees allocated to Elections Canada.

10.20 In the same way as the government appoints returning officers, the two parties or candidates that came first and second in the previous election are given the right to nominate urban enumerators. The returning officer must accept and train these nominees unless there are good reasons for not doing so.

10.21 Although this ensures that the principal political interests are represented in the process and provides some assurance that elections are fairly and impartially conducted, there are drawbacks. For example, candidates often give the returning officers their lists of nominees late and, most of the time, the number of names is fewer than needed. This complicates the task of the returning officers who, at the last moment, in the midst of election preparations, have to find people for the positions and train them if there is time. The Chief Electoral Officer has no control over these matters which nonetheless affect the efficiency of the electoral machinery.

Outdated legislation: a major problem

10.22 The success of the Chief Electoral Officer and Elections Canada can be judged by their ability to satisfy the electoral requirements of the Canada Elections Act, namely: to meet all the specified activity deadlines throughout the election period, to hold an election on the appointed date, to promptly report the results, and to manage the associated human, financial and materiel resources appropriately. All this is to be done in compliance with the law, fairly and impartially and in conjunction with returning officers.

10.23 The present Canada Elections Act is a lengthy and disorganized composition which in many instances specifies administrative procedures to the smallest detail. The authorizing legislation for other agencies is often expressed in broader terms to allow the appointed agency heads an adequate level of administrative flexibility to meet their program objectives. The Canada Elections Act allows very little discretion.

10.24 Moreover, electoral procedures under the Act have not been amended in substance for many years and consequently do not reflect recent social and technical developments which bear on the electoral process and significantly affect its costs. The environment has evolved; the legislation controlling the electoral process has not.

10.25 Since 1980, the Chief Electoral Officer has drawn attention to the likely impacts on the electoral process if legislative action is not taken. His most recent statutory report spoke of a crisis in election administration. He has noted the rising number of complaints and has indicated that public distrust of the electoral machinery could result.

10.26 The Chief Electoral Officer, although given some discretionary power during an election, has little flexibility between elections to make administrative improvements to the electoral process. By way of comparison, some provinces do grant their Chief Electoral Officers a certain amount of flexibility.

10.27 Examples of demographic and social changes in Canada that have occurred and that have an impact on the legislation are the significant number of Canadians travelling or living abroad who wish to vote but cannot, and a mobile and urban population becoming increasingly difficult to enumerate. Other changes are associated with the effect the *Charter of Rights and Freedoms* has had on the Canada Elections Act. Interested citizens such as judges, prison inmates, the handicapped, and supporters of freedom of expression have challenged the Act, sometimes successfully. Those successes have in turn called into question some of the assumptions underlying the Canada Elections Act.

10.28 The outdated legislation has also led to inefficient procedures and higher costs in administering the electoral process. One example is the ballot box. Metal ballot boxes, which appear to be required under the Act, cost $500,000 more to use at a federal election than cardboard boxes (see Example 1).

Example 1

Ballot Boxes: High Costs

10.29 The following illustrates one of the many difficulties Elections Canada faces in administering the present legislation with the inefficiencies it creates. It also shows the need for better financial management and control.

10.30 Cardboard ballot boxes are now being used by some provincial administrations. Granted, they are usable only once, but they require one-way shipping only, no maintenance and are easier than metal boxes to handle and move about between storage depots and polling stations.

10.31 The Canada Elections Act says that "each ballot box shall be made of some durable material...". Other parts of the Act specify that locks, keys, and metal seals should be used in relation to the box. Elections Canada had interpreted this to mean that it could use only metal ballot boxes.

10.32 In anticipation of proposed amendments to the legislation announced by the government in 1987, which would have permitted greater flexibility in this area, Elections Canada began to dispose of its metal ballot boxes and to purchase cardboard ones. However, the legislation was not amended. As a result, there was a shortage of metal boxes at the time of the November 1988 election and Elections Canada was required to use cardboard ballot boxes in Ontario and Quebec.

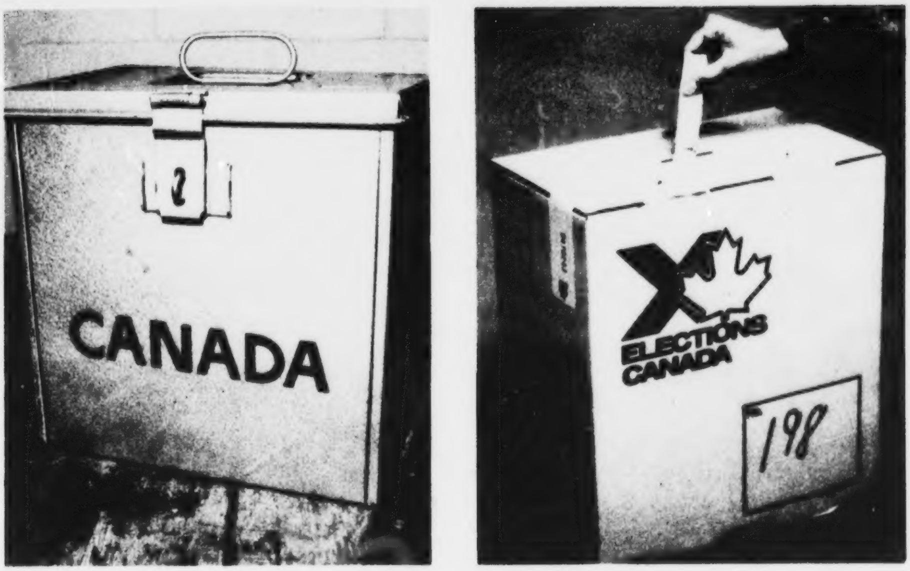
10.33 Elections Canada estimates that at each election a metal ballot box costs $10 to use compared with $2.50 for the cardboard ballot box (see photo). Some 40,700 cardboard ballot boxes were used, at a cost of $102,000. Although this technically violated Elections Canada's interpretation of the existing legislation, it resulted in savings of $305,000 based on the difference in cost between metal and cardboard boxes. Had cardboard boxes been used throughout the country, additional savings of $207,000 would have been realized.

10.34 Even so, Elections Canada did not pay due regard to economy in purchasing the cardboard ballot boxes:

- 60,000 of the boxes were purchased between October 1987 and September 1988 for $135,000, or $2.25 each. The contract was let without competitive bidding and there was no evidence that any detailed cost or needs analyses had been carried out. Two provinces using cardboard ballot boxes pay $0.88 and $1.75 for each of their boxes.
- One million paper seals were purchased for the cardboard ballot boxes, but only 688,000 seals were used. The purchase exceeded requirements by $22,000. Furthermore, because the seals have a shelf life of only three years, it is likely that the remainder will be unusable at the time of the next federal election.

10.35 Another example is the necessity to return to Ottawa a substantial portion of the 600 tons of material shipped out to service the election. Some of this material includes voting records returned to Ottawa for storage and security. The remainder of the material may include excess supplies and some used material that might be recycled. Moreover, the Act requires the return of much of this material by registered mail. One section of the Act alone calls for the return by registered mail of the following documents: the report of proceedings; polling station recapitulation sheets; poll statements; the unused supply of ballot paper;

A contrast in ballot box usage costs for the 1988 election (see paragraph 10.33).



Metal: $10.

Cardboard: $2.50

enumerators' record or index books; revision documents; returns from the various polling stations including poll books, unused ballot papers, ballot papers cast, spoiled ballot papers, rejected ballot papers, the official list of electors; and agent information.

10.36 Moreover, the election writ that carries the endorsement of the returning officer showing which candidate received the majority of votes, and was thus elected, must be returned by registered mail. It cannot be officially transmitted by other sure, faster means, such as FAX.

10.37 In June 1987 the government introduced Bill C-79 in the House of Commons, proposing amendments to the Canada Elections Act and related legislation. This Bill died on the Order Paper when the Thirty-third Parliament was dissolved. More recently, in the April 1989 Speech from the Throne the government announced that a commission of inquiry would be established to make recommendations for needed changes and reforms to the electoral laws. At the conclusion of this audit in June 1989, the commission had not yet been established.

Returning officers: appointment process flawed

10.38 The returning officers, who administer the Canada Elections Act in each of the current 295 electoral districts, are pivotal figures in an election.

10.39 Before the election, their preparation responsibilities include several tasks. They must undergo training when appointed or when the legislation changes. They plan the electoral administration of the district so that they can respond properly when the election writ arrives. This includes dividing their electoral districts so that polling stations are distributed fairly and provide easy access to the electorate. They receive, store and distribute large quantities of supplies sent from Ottawa.

10.40 When the election is called, returning officers must immediately find office space, arrange for administration, telephone service, staff training, elector enumeration; receive candidate papers; and institute financial and other management controls. They must also maintain contact with the representatives of the candidates and political parties involved. Finally, they must be ready to provide information to the general public and the media. All this has to be accomplished in as little as seven weeks, following specific daily goals required by the law. After the election they have to settle their accounts with Elections Canada and with their workers, and satisfy other important election requirements.

10.41 Returning officers for each electoral district are selected and appointed by the Governor in Council, on the recommendation of the responsible minister (currently the President of the Privy Council). The officers are paid for their services according to a tariff of fees approved by order in council. There is no annual salary or other remuneration attached to the office. The average fee received by returning officers during the 1988 election was about $12,700.

10.42 Based on its electoral experience, Elections Canada has set out the responsibilities of returning officers, along with suggested guidelines for their selection. Contact between the Government and the Chief Electoral Officer on the selection of returning officers is rare, and this can lead to the appointment of individuals less qualified than required. This in turn affects the efficiency of the electoral operations. Elections Canada accumulates information on the performance of returning officers but has no performance measures in place by which they can be objectively evaluated. This information is not passed to the government.

10.43 When a returning officer dies, resigns, or is removed from the position for cause, the Government has sixty days in which to appoint a replacement to the office under the Canada Elections Act. There is no such time limit in place when a new electoral district is created as a result of redistribution. The creation of the new districts in effect terminates the previous returning officer appointments.

10.44 When the current electoral boundaries were proclaimed on 13 July 1987, 282 new ridings were created and therefore 282 vacancies were created for returning officers. Thirteen electoral districts remained unchanged.

10.45 One hundred and seven days elapsed before the first returning officers were appointed on 28 October 1987. Then only 54 of the required 282 appointments were made. The last four returning officers were appointed on 18 September 1988, about two weeks before the November general election was called.

10.46 The delay in appointments made it difficult to plan for the training of inexperienced returning officers, amounting to 85 percent of appointments for the 1988 election. It also shortened the planning time available to the returning officers to prepare for their upcoming responsibilities.

Enumeration and revision: still a largely manual process

10.47 Reduced to basics, federal enumeration is a two-stage data gathering and processing exercise conducted during the election period. In the first stage urban enumerators visit homes, apartments, and other residences to obtain and record the names of those who are qualified to vote. Along with residential visits, rural enumerators may secure elector information from other available and convenient sources. The second stage sees the transfer of this information, mostly by hand, on to voters lists, enumeration notices and other election documents. The elector's name is transcribed manually at least 5 times on various documents before the vote is cast.

10.48 Revision is an amending process whereby electors who were missed during the enumeration stage may get their names added to the list of voters.

10.49 Enumeration and revision are formidable administrative tasks and highly labour-intensive, comprising the single largest cost component of an election. For the November 1988 election, total field costs in the constituencies were estimated at about $75 million. About half of that is estimated to be the cost of enumeration and revision -- up 15 percent in dollar terms from the previous general election in 1984.

10.50 The June 1986 White Paper on Election Law Reform reviewed the possibility of having a permanent voters list but rejected it as being too costly and less accurate than the present method of compiling voters lists.

10.51 Although the existing legislation does contribute to administrative inefficiencies in the process, there are opportunities for improvements in the present system, particularly in the use of technology. For example, Elections Canada could issue a standard data processing software package for use, where locally feasible, instead of simply describing system requirements as is done now. In the last general election, some returning officers lightened their workload by hiring data processing firms to prepare the list of electors and the enumeration notices for the second stage of the process. For instance, several Toronto area ridings combined to use a local data processing firm to carry out major election tasks. But in the majority of the ridings most of the work was still done manually.

10.52 Elections Canada has attempted to introduce computer technology in a number of areas. For instance, returning officers were provided with computer terminals for the duration of the 1988 general election and most correspondence between Elections Canada headquarters and the ridings was conducted through electronic mail.

10.53 However, we found that Elections Canada had not comprehensively examined the potential savings and gains in efficiency associated with using information technology nationwide in enumeration and revision. The benefits could be significant.

10.54 Elections Canada should continue to explore ways to introduce up to date technology in all aspects of the electoral process, and to encourage its use by returning officers.

Management's response: *We will continue to explore ways of introducing new technology in areas of our operations where potential savings may be realized. Also, we will be looking into the feasibility of developing a standard data processing software package for the use of returning officers in preparing the preliminary lists of electors.*

Elections Support

10.55 We reviewed two of the major support activities of Elections Canada -- the supply of election material and training. We also reviewed the important administrative functions of the organization including financial administration, contracting, and general planning and analysis. At the time of our audit, the Public Service Commission was also reviewing staffing procedures.

Planning and Organization

Planning in uncertainty leads to crisis management

10.56 Planning for elections is planning in uncertainty. In the parliamentary system, a general election can be called at any time, as can a by-election (which generally uses the same process as a general election). For this reason the electoral machinery has to be kept ready to start immediately. This tends to impose on any electoral organization a sense of impending emergency. With each election seen as a crisis, as something to be reacted to, the value of planning and analysis can sometimes be overlooked.

10.57 Since 1957 Canadians have elected six minority governments, during the course of twelve general elections. Moreover, since 1980 Elections Canada has twice been involved with the redistribution of electoral districts, an activity that routinely occurs once a decade These levels of electoral uncertainty and activity have disrupted Elections Canada's planning.

10.58 It also becomes more difficult to plan when there is reason to believe that elections legislation may be amended, as was the case in 1988. Preparations for the November 1988 general election were inhibited by the expectation that Bill C-79 would amend the Canada Elections Act and rectify or lessen various problems. This did not happen. But, while waiting and trying to plan the election, Elections Canada struggled with the following scenario. If Bill C-79 were passed, the Act would change the nature of the instructions to returning officers, the training program, the forms and papers used in the election, etc. A major consideration was whether there would be enough time to make the administrative changes before the next election. Further, and depending on the date of the general election, it was uncertain what group of returning officers -- the old or the new -- would be in place which had to be taken into account for their training.

10.59 The uncertainty of 1987 and 1988 continues into the future. The 1991 decennial census is approaching quickly and will be followed, probably in 1992, by an adjustment of the electoral boundaries. A commission of inquiry is to be conducted. The life of the present Parliament expires in late 1993, at which time -- and more likely before -- a general election must be held. Conceivably, Elections Canada may find itself in the same position it was in before the November 1988 general election: again faced with training two sets of returning officers; planning two different sets of electoral districts; and converting two sets of laws into the necessary detailed instructions.

10.60 The effect of these uncertainties in a crisis atmosphere has been to focus Elections Canada's attention on meeting the requirements of the Canada Elections Act. Other considerations such as analysis, planning, and financial management matters, involving Elections Canada's internal administration, have received less attention.

Informal organization approach no longer adequate

10.61 Historically, Elections Canada has grown slowly in its size and its responsibilities. Originally a small unit concerned strictly with running the electoral machine, today it includes a financial group that pays the organization's expenses and supervises the reimbursement of millions of dollars of election expenses to candidates and political parties; a Broadcasting Arbitrator who is concerned with broadcasting provisions during the election period; a Commissioner of Canada Elections who deals with complaints; and Elections Canada which is responsible for the administrative process supporting changes to electoral boundaries.

10.62 Throughout the past 15 years, these new responsibilities have been calling for a greater emphasis on the management of the overall process, where running the electoral machinery is just one of the important elements. Neither the legislation nor the internal arrangements have been modified to permit the organization to meet this new managerial requirement.

10.63 Partly as a function of size, Elections Canada has worked until recently in a project management style where different parts of the organization contribute to the progress of individual projects. But it has not assigned responsibilities for projects or activities clearly enough. For example, no one is assigned conclusive budgetary and program responsibility for training returning officers, or for setting the tariff of fees. Indeed, until December 1988 the formal organization chart did not reflect the actual organizational relationships.

10.64 Little use is made of budgets, and financial reports are inadequate. File systems in some areas are not well developed. Documented reasons for taking one or another course of action are difficult to find as was the case with the Voter Inquiry Services (see Example 2). Financial control on the electoral side concentrates on the payment of accounts and election expenses.

Example 2

Voter Inquiry Services: Better Analysis and Planning Required

10.65 The following illustrates the effect that unclear legislation, contracting procedures and limited planning and analysis had on Elections Canada's provision of a voter inquiry service.

10.66 Taking into account the electoral boundary changes and the almost complete turnover of returning officers Elections Canada decided, for the 1988 general election, to establish a telephone answering service -- centralized and decentralized -- to dispense information to callers on voters' rights and on how these might be exercised. The organizing principle created a two level service to handle uncomplicated questions at the local level with more difficult ones to be referred to Elections Canada in Ottawa.

10.67 The provision of these services was based on the Chief Electoral Officer's conviction that citizens have a right to be informed about their constitutional right to vote and of the means by which they can access that right. Elections Canada has sought an amendment to the Canada Elections Act to give that conviction a legislative basis.

10.68 Elections Canada's telephone answering service began working on 26 August 1988. In Ottawa, a staff of approximately 10 was linked to all regions of Canada by a toll-free number and their work hours were adjusted to accommodate Canada's population living in six time zones. This unit was managed by the Communications Division of Elections Canada.

10.69 As a possible election drew nearer a sole-source contract for the decentralized service was signed on 23 September 1988. The contractor was Reference Canada, a unit within the Department of Supply and Services. Reference Canada provided the service through its offices and by affiliation with established telephone inquiry units providing similar services to provincial governments and other organizations.

10.70 We noted that documentation related to issues such as mandate, need (including assumptions) and costs was not well organized in explaining systematically the development of the service.

10.71 The contract with Reference Canada made satisfactory provision for quality control to be exercised over the information provided to those using the service. However, the amount paid per call to Reference Canada was based on figures it gave to Elections Canada. These were not challenged by examination. There are also significant differences in the costs for these two services from the viewpoint of the total calls handled.

Organization	Total Cost	Total Calls	Cost per call
Reference Canada	$ 349,700	73,900	$4.73
Elections Canada	$ 121,600	44,300	$2.74

Although the costs are not strictly comparable, the rate paid under the contract with Reference Canada was considerably higher than Elections Canada's in-house costs.

10.72 The Inquiry Service of Elections Canada collected information on complaints made by callers. At the time of our audit we noted Elections Canada had not undertaken detailed reviews of the logs to determine the nature and source of problems in the election that generated complaints, with a view to making changes for future elections.

10.73 The organization realizes its informal work arrangements are no longer serving it adequately and is taking steps to clarify its responsibilities.

10.74 Elections Canada should adopt a more formal approach in its work and place greater emphasis on planning, analysis and documentation in all aspects of its work.

Management's response: *To the extent feasible, within the limitations of the uncertain environment and our limited human resources, we will take the necessary steps to foster better planning, analysis and documentation of our work at all levels of the organization.*

Election Supply Management

Room for improvement

10.75 General elections require large amounts of election supplies -- about 600 tons -- which are assembled in Ottawa and then distributed across the country to the 295 returning officers (see photo). Much of the material that is shipped out is returned to Ottawa after the election, as required by the Canada Elections Act, for safekeeping, re-use, or disposal.

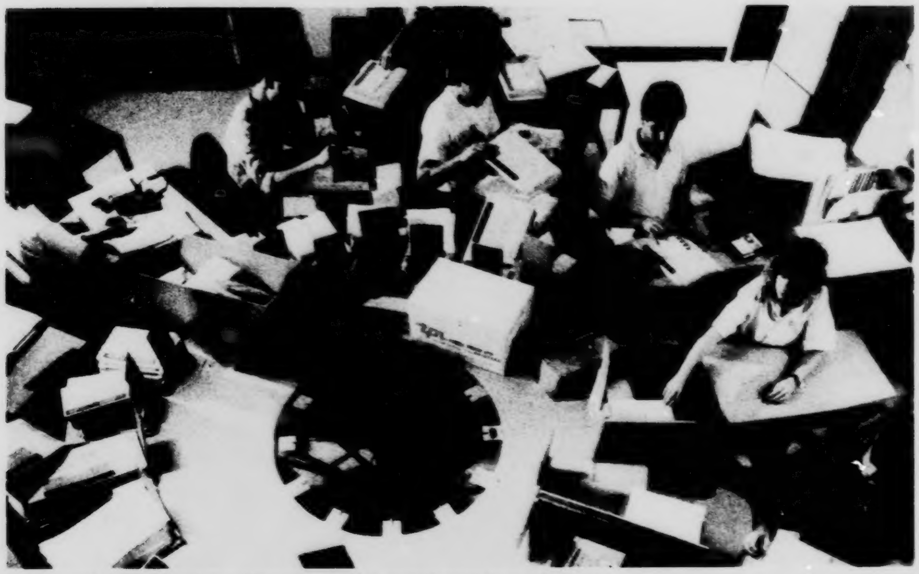
10.76 Elections Canada has a good system for estimating the quantities of supplies needed. Quantities of each item are determined with the aid of a computer system and are based on the number of people, candidates, and polling divisions in each electoral district. The amounts shipped are based on historical usage patterns and are updated from the most recent statistics. Between elections, supplies are replenished over a 32-month planning cycle. Factors such as lead times, the cost of acquiring and carrying materiel and the likelihood of an election being called are taken into account during this process.

10.77 While blank ballot paper is well protected, warehouse security in Ottawa is inadequate. One of the assumptions the Canada Elections Act appears to make is that election records can be better safeguarded in Ottawa. The assumption may be unjustified. The used ballots, voters lists, and other confidential material in the Elections Canada warehouse, for example, are easily accessible through unlocked doors. Visitors are not challenged by employees. At the time of the audit, some employees smoked in the warehouse in these combustible conditions, in an apparently smoke-free government building. This was brought to the attention of management and the practice has stopped.

10.78 Moreover, the principal warehouse, at 51,000 square feet with a 3,000 ton capacity, is larger than necessary for the approximately 1,000 tons that is accumulated before general elections.

10.79 For some time the Treasury Board Secretariat has recommended that Elections Canada consider privatizing the warehouse with a view to achieving economies. On 1 June

Packaging of election supplies: 600 tons were handled in 1988 (see paragraphs 10.75 and 10.76).



We found that Elections Canada had a good supply system.

1989 Elections Canada contracted for an effectiveness and efficiency review of the warehouse operations. Another alternative would be to decentralize operations.

10.80 Materiel other than election supplies is inadequately estimated and controlled. Electoral maps are a good example. There are still large quantities of maps in storage, not being used, which date back to 1974. No assessments or cost analyses have been made of the value of the current inventory, the cost of storing it, or alternatives.

10.81 Elections Canada should improve its supply management system by:

- **strengthening warehouse security procedures;**
- **examining more cost effective alternatives for the warehouse operation; and**
- **establishing better control of its miscellaneous supplies.**

Management's response: *The report on the effectiveness and efficiency review of the warehouse, when received, will provide this Office with the information necessary to decide on the future organization and function of this service. Also, within the context of the federal government security policy, we will be undertaking in the near future a complete threat and risk assessment of the premises we occupy, including the warehouse.*

Training

Satisfactory systems and procedures

10.82 One of the most significant support activities of Elections Canada is training returning officers and, indirectly, other election officials across Canada. Returning officers have to be trained first. Then, during the election period, in two successive training periods of less than a week, returning officers must first train close to 100,000 enumerators and other election workers and then, subsequently, another approximately 100,000 workers made up of deputy returning officers and poll workers.

10.83 We reviewed the systems and procedures Elections Canada had in place to carry out its training activities for the 1988 election, prior to which it had been faced with issues having a significant impact on its training program.

10.84 First, delays in appointing returning officers meant that training had to be squeezed into a short period. This complicated planning, training, operations and the monitoring tasks of Elections Canada and may have led to increased inefficiencies in the constituencies. To complete the training on time Elections Canada had to incur additional problems and costs.

10.85 Second, it could not be anticipated whether new legislation arising from Bill C-79 would be forthcoming. Depending on timing, new legislation could have overridden earlier training and related preparations. Third, in the 1988 general election over 85 percent of the returning officers were inexperienced.

10.86 In spite of these difficulties, the systems and procedures for training returning officers and electoral staff were generally satisfactory. Senior management was involved throughout and improvements had been made in the quality and quantity of training and support materials since the previous election.

10.87 In less than a year Elections Canada trained about 320 persons for 295 returning officer positions. There were no significant procedural failures in the elections.

Financial Management and Control

Ongoing costs are generally well controlled

10.88 The ongoing costs of administering the Elections Canada organization ($2.5 million in 1988-89) require parliamentary approval and are subject to Treasury Board scrutiny.

10.89 Financial management and controls over these ongoing costs are generally satisfactory.

Election costs: limited controls and little analysis

10.90 The costs of running an election are statutory (an estimated $120 million for the November 1988 election) and do not require parliamentary approval. The costs are reported to Parliament through the Estimates, the Report of the Chief Electoral Officer, and the Public Accounts.

10.91 In our opinion, Elections Canada does not have sufficient information or systems in place to enable it to determine what an election should cost and whether expenditures are made with due regard for economy and efficiency.

10.92 Except for the reimbursement of candidate and party expenses (about $20 million for the 1988 election), financial management and controls over election costs are weak:

- Senior managers are not held accountable for financial resources.
- There is no systematic and periodic analysis and reporting of the major components of the election process, nor do the limited financial systems provide the information that would permit an in-depth analysis. As a result, managers are often not aware of the costs of these activities. For instance, training of returning officers and other electoral officials is an important step in the electoral process. Elections Canada staff informed us that they thought training costs for the 1988 election were less

than $1 million; our analysis indicated that the costs were about $4 million. In fairness, what the audit identified as training costs may not have coincided with the training costs as understood by Elections Canada staff.

10.93 Under the Act, returning officers have only to certify that expenses are valid to have them paid. Adequate analysis is not undertaken after the election, by riding, to compare expenditures of returning officers and to understand the reasons for variances, or to identify opportunities for savings. Nor have benchmarks, such as cost per elector, been established against which these costs can be monitored. Returning officers spend on average upwards of $250,000.

10.94 Little comparison of costs with other electoral jurisdictions is done. Although the processes are not identical, they are sufficiently similar to allow investigation and comparison, with useful insight to be gained into one's own practices. Based on information we obtained from seven provinces, the cost per voter in the last provincial election ranged from $2.31 to $8.00 compared to an estimated $6.85 for the 1988 federal election.

Outdated legislation has led to inefficient and costly procedures in administering the electoral process. Preoccupied with these problems, management has paid insufficient attention to analysis, planning, financial management and organization.

10.95 The tariff of fees that governs over 60 percent of the field expenditures is unwieldy in its complexity. The tariff structure, approved annually by order in council after review by the Department of Justice, sets the fees, costs, allowances and expenses to be paid to returning officers and other officials specified by the Act. The tariff of fees details the majority of tasks in the electoral process, from the hiring of messengers to the printing of ballot paper.

10.96 The updating of the tariff by Elections Canada staff has focussed on increasing fees and allowances to reflect the consumer price index. Insufficient emphasis has been placed on whether the various individual tariffs reflect current needs or reasonable costs. For instance, data processing costs for preparing electoral lists became a permissible item in the tariff of fees for the first time in the last general election. However, no analysis was done of what a reasonable amount should be. The fee permitted was identical to that for processing the lists manually.

10.97 The lack of adequate financial management and control over election costs is due in part to the informal nature of the organization, and the emphasis it places on quality of service and the delivery of an election result. In addition, during and immediately after the election most of the organization's financial efforts have been directed to the control and review of candidate and party expenditures, with the result that inadequate emphasis has been placed on monitoring other significant areas of election costs. It is incumbent on the organization to have in place the best possible analysis and financial management and control systems.

10.98 Elections Canada should strengthen its financial management and control systems for planning, recording, controlling and reporting on the costs of running elections.

Management's response: *In the near future we will begin to develop a new code of accounts which will serve as the basis for the development of a new comprehensive management information system for election costs covering both headquarters and returning officers' offices. Better analysis of the cost of activities will also be given priority consideration.*

Contracting: poor procedures and controls

10.99 Elections Canada contracts for a variety of goods and services such as election supplies, computer systems and consultants, artwork, and graphics. Although the Chief Electoral Officer is not subject to government contract regulations, the organization has resolved nevertheless to follow their spirit and intent.

10.100 Our examination has shown that frequently this is not happening. For instance, we found that:

- in a number of instances, a formal competitive bidding process is not followed. This may have resulted in higher costs than necessary as illustrated in Examples 1 and 2.
- not all contracts specify a total dollar value and/or dates during which the delivery of goods or the performance of services must occur.
- needs analyses, ordering instructions from program managers, and other substantiating information to support negotiation and finalizing of contracts are not usually available.
- no comprehensive list of contracts was available when we conducted our examination. We were unable to accurately confirm the extent of the commitments or the amounts spent, although we estimate them to be in the millions of dollars.

10.101 Elections Canada should improve its contracting procedures.

Management's response: *We are in the process of updating our contract policy which will cover the shortcomings mentioned above. Also, we will develop a contract register to provide better control of our contractual commitments.*

Internal audit: limited activity

10.102 Other than the intensive reviews of party and candidate expenses carried out under the direction of the Elections Canada financial group, there have been no recent financial audits of other activities in Elections Canada. Given the sensitivity of its activities and the high profile it receives, Elections Canada would be well advised to introduce an internal audit function. With the peaks and valleys in activity this audit function could, for example, be contracted out.

10.103 Elections Canada should introduce an internal audit function.

Management's response: *We agree. Arrangements have been made with the Audit Services Bureau of DSS to develop an internal audit policy and a 5-year audit plan. Work is to commence in the Fall of 1989.*

Reporting to Parliament

10.104 The Chief Electoral Officer reports at the beginning of each session to the Speaker of the House of Commons on the administration of his office, and is also required to suggest amendments to the Canada Elections Act that will improve its administration. Through Part III of the Estimates the Chief Electoral Officer also reports comprehensively on the expenditures of Elections Canada and its administration.

10.105 In general the information provided to Parliament on the activities of Elections Canada is adequate. We did note, however, that tax credits to donors, which are part of the cost of elections and which approximated $44 million from 1984 to 1987, are not reported to Parliament.

10.106 Elections Canada should undertake discussions with the Department of National Revenue - Taxation with a view to reporting the cost of election tax credits to Parliament.

Management's response: *We agree. We will be contacting Revenue Canada-Taxation to determine the most appropriate method of publicly reporting the cost of tax credits.*

Co-ordination With Other Electoral Offices

Potential for significant savings

10.107 There are many similarities in the election processes of various levels of government in Canada. For example, other jurisdictions must identify voters, prepare voters lists, use ballot boxes, arrange for polling stations, develop street indexes, provide for secrecy and security of the ballot, count and report the results. Each of these costly systems is supported separately by the same group of taxpayers within a given geographic area.

10.108 Given the commonality of electoral tasks, and given some of the technical innovations developing across all jurisdictions, there appears to be significant potential for sharing information on common systems and procedures in such areas as mapping, enumeration, computerization, warehousing, and the production of forms and ballot boxes. This could result in annual savings of tens of millions of dollars across all jurisdictions.

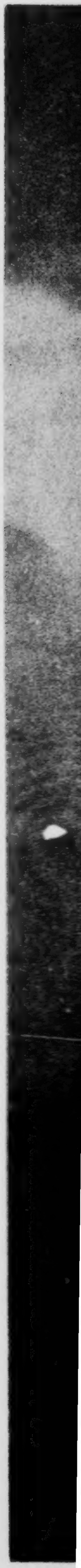
10.109 Elections Canada, in co-operation with its counterparts in other jurisdictions, should investigate the feasibility of developing common systems and procedures for the administration of elections in Canada.

Management's response: *We agree. Elections Canada has been meeting with election officials from the 10 provinces and two territories on an annual basis for the past 15 years to explore areas of mutual interest and cooperation within the constraints of our respective legislation. Furthermore, at the July 1989 conference, all jurisdictions agreed to a proposal put forward by Elections Canada to organize a number of consultative committees on specific issues such as, fees paid to and terms of employment of returning officers and the development of computerized mapping systems.*

11

DEPARTMENT OF THE ENVIRONMENT

Canadian Parks Service



11

DEPARTMENT OF THE ENVIRONMENT

Canadian Parks Service

Main Points

11.1 The Canadian Parks Service (CPS) is responsible for protecting significant examples of Canada's natural and cultural heritage for all time and providing public access to this heritage in ways that do not impair its integrity (paragraphs 11.7 to 11.9).

11.2 Improvements to a number of management planning and control systems have been started, but implementation of most of these systems has been slow. The Canadian Parks Service lacks a strategic plan to provide guidance and coherence to these various efforts. Many of the problems we observed in our 1983 audit and 1985 follow-up still remain (11.17 to 11.21).

11.3 The Canadian Parks Service has developed and uses a well designed planning procedure to ensure that the diverse natural regions of Canada will be represented in our national parks system. However, because there is no time-frame for completing the system, there is a danger that opportunities to establish parks in some natural regions may disappear before the national parks system can be completed (11.23 to 11.31).

11.4 Although the program evaluation function has existed since 1978-79, the first evaluation study is not scheduled until 1992. In addition, the Canadian Parks Service continues to lack reliable measurement of attendance statistics. More than 10 years will have elapsed before recognized deficiencies are corrected. A performance measurement information system is expected to be ready for 1994 (11.32 to 11.39).

11.5 Within the parks, procedures have been developed to protect the natural resources. However, in the parks we visited these natural resource management procedures were not being implemented, even for plants and animals recognized as high priority (11.40 to 11.50).

11.6 Opportunities exist to improve the productivity of a number of overhead activities, and to reallocate resources to meet potential shortages in operational areas (11.68 to 11.88).

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- Inadequate information for Parliament and management (11.108)

Exhibits:

11.1 Canadian Parks Service - Organization Chart

11.2 Parks Program - 1988-89 Resources

11.3 National Parks' 39 Natural Regions - Almost half of the natural regions are not yet represented

11.4 Park Management Plan - Resource Management Plans are not prepared for high priority natural resources

DEPARTMENT OF THE ENVIRONMENT

Canadian Parks Service

Background

11.7 The Canadian Parks Service (CPS) is a major program of the Department of the Environment. The objective of the Parks program is "to protect those places which are significant examples of Canada's natural and cultural heritage for the benefit, understanding and enjoyment of the people of Canada, in ways which leave that heritage unimpaired for future generations".

11.8 Part III of the 1988-89 Estimates reports that CPS administers 34 national parks, 83 national historic parks and major historic sites, 9 heritage canals, 5 heritage rivers and 2 co-operative heritage areas.

11.9 Natural heritage is concerned with the physical features, plants and animals of our country; cultural heritage is concerned with certain physical reminders of important people, places and events in Canadian history. Systems of national parks and historic sites are being developed by CPS to protect examples of our natural and cultural heritage.

11.10 The Canadian Parks Service is governed by a number of statutes including the Department of the Environment Act, the National Parks Act, the Historic Sites and Monuments Act and the Department of Transport Act. The Parks program's mandate dates back to 1887; the most recent amendment to the National Parks Act, in 1988, was to strengthen its ability to preserve Canada's natural heritage and ensure that it is used with care.

11.11 The Canadian Parks Service's organizational structure is shown in Exhibit 11.1. The 1988-89 person-years and expenditures for the Parks program are shown in Exhibit 11.2.

11.12 The Canadian Parks Service has been under resource constraint since our 1983 audit. Person-years have remained relatively constant. Operation and maintenance budgets, in 1984-85 dollars, have not changed significantly. During the same period CPS' capital budget, in 1984-85 dollars, decreased by approximately 17 percent. The addition of five new national parks in this period has put further pressure on available resources.

11.13 The Canadian Parks Service is responsible for managing certain assets which it feels are not directly related to its mandate. The Service believes this deflects resources away from other assets which contribute more directly to the Parks program objective. For example, CPS is responsible for maintaining roads which are used as national highways. Maintenance expenditures on these roads, which must be open year-round, account for about 10 percent of total expenditures on assets maintenance. This puts considerable pressure on the person-years and dollars available for maintaining other assets, for providing services to visitors and for important resource conservation activities.

11.14 In 1988 the Treasury Board requested that the Departments of Environment, Public Works and Transport review their respective responsibilities for expenditures on highways in national parks. This review had not been completed at the time of our audit.

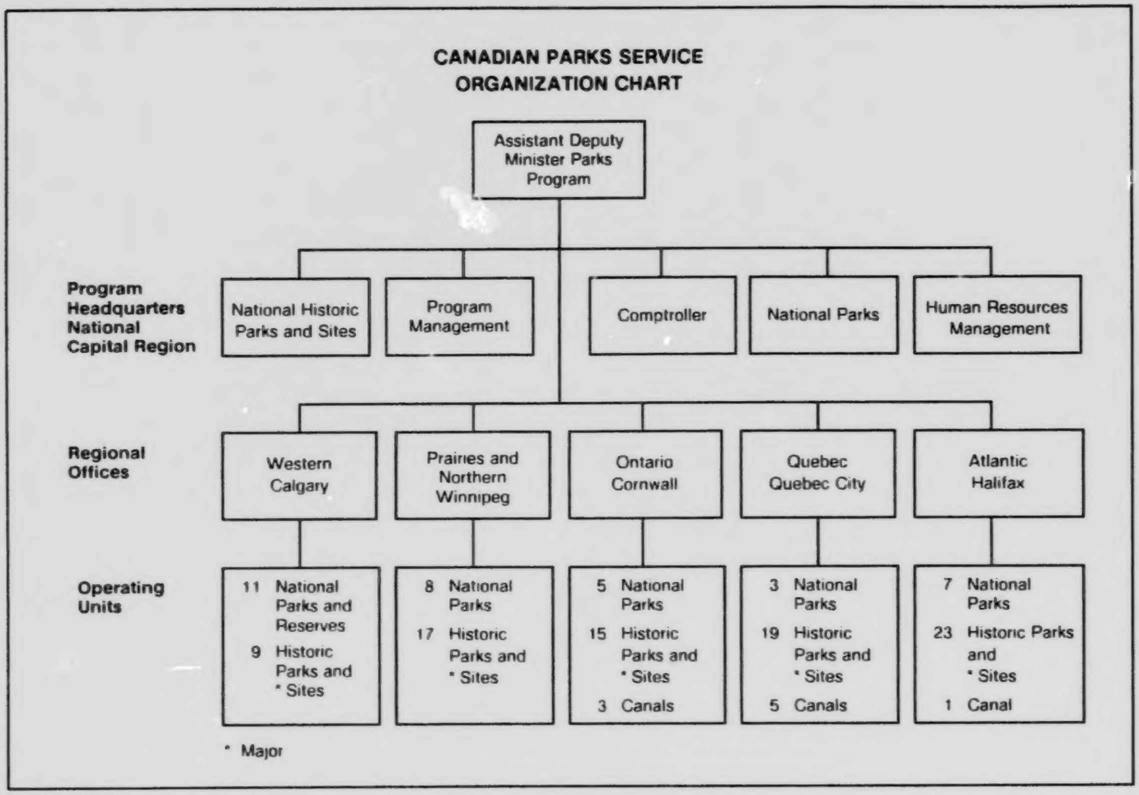

CANADIAN PARKS SERVICE
ORGANIZATION CHART
Assistant Deputy Minister Parks Program
Program Headquarters National Capital Region
National Historic Parks and Sites
Program Management
Comptroller
National Parks
Human Resources Management
Regional Offices
Western Calgary
Prairies and Northern Winnipeg
Ontario Cornwall
Quebec Quebec City
Atlantic Halifax
Operating Units
11 National Parks and Reserves
9 Historic Parks and * Sites
8 National Parks
17 Historic Parks and * Sites
5 National Parks
15 Historic Parks and * Sites
3 Canals
3 National Parks
19 Historic Parks and * Sites
5 Canals
7 National Parks
23 Historic Parks and * Sites
1 Canal
* Major

Exhibit 11.1

Audit Scope

11.15 Our 1983 audit of CPS focussed on key aspects of operations. These included new park acquisitions, program management information, management of professional staff and revenue policy. In 1985 we reported on action taken in response to our 1983 observations and recommendations. In this audit we revisited many of the same areas. Specifically, we concentrated on the following aspects of program management:

- **Strategic planning.** We examined strategic and operational planning procedures.
- **Performance measurement and reporting.** We examined:
  - the implementation of policy and procedures for land-based national park system planning;
  - the policy and procedures for obtaining and using attendance statistics; and
  - the major approaches used by CPS for the ongoing and periodic measurement of program effectiveness.
- **Protecting natural resources and physical assets.** We examined:

PARKS PROGRAM
1988-89 Resources

	Person-Years	Operations ($000's)	Capital ($000's)	Grants and Contributions ($000's)	Total ($000's)
Program Activities					
Parks Operation	3,693	$ 175,155	$ 66,735	$ 994	$ 242,884
Parks Development	370	19,126	20,037	23,905	63,068
Program Management and Technical Services	615	45,581	9,670	-	55,251
TOTAL	*** 4,678**	**$ 239,862**	**$ 96,442**	**$ 24,899**	**$ 361,203**

* Excludes 226 person-years transferred to the Department of Public Works in 1988-89

Exhibit 11.2

- the protection of natural resources through the implementation of Natural Resource Management Plans which cover parks' plants, animals and natural features;
- the management of the in-service stage of physical assets, such as buildings, utilities, campgrounds, trails, roads, canals and major equipment.

- **Managing the efficient use of human resources.** We examined:
  - the extent to which service quality has been maintained during a period of resource constraint; and
  - the extent to which CPS minimizes organizational layering and overhead and administrative burdens.
- **Managing revenue and cost recovery.** We examined:
  - compliance with Treasury Board and CPS cost recovery policies; and
  - fee establishment and collection procedures.
- **Managing informatics.** We examined the functions and activities designed to achieve efficient and effective use of information technology within CPS.

- **Information for Parliament.** We examined the quality of information provided for Parliament in Part III of the 1988-89 Estimates.

11.16 Several CPS activities receive functional direction from the Department of the Environment's corporate organization. These activities include informatics management and financial management and control. We plan to report on DOE's corporate functional direction in these and other areas in 1990.

Observations and Recommendations

Strategic Planning

There is a need for a strategic plan

11.17 CPS has not prepared a strategic plan to guide the allocation of the Parks program's budgetary resources to meet strategic objectives. A strategic plan would require the Service to articulate the program's role. It would be an analysis of the environment, a statement of long-term objectives, and a strategy for achieving those objectives. It would identify priorities and associated resources as well as a time-frame and tactics. Such a plan would not be static; it would have to be adjusted to changing circumstances. Nevertheless, it would serve to provide a common vision and guidance to all program personnel.

The objective of our audit was to determine whether CPS has adequate measures of program effectiveness, the program is managed economically and efficiently and Parliament is kept informed of results.

11.18 A strategic plan provides a consistent basis for determining the proportion of resources to be allotted to the various components of the program. There are many competing demands. National parks compete with national historic parks and sites for scarce resources, operations with capital, resource conservation with visitor activities and park establishment with park development. Not establishing priorities for such demands in an environment of scarce resources risks seriously weakening functions central to the program objective in order to maintain less important functions or facilities.

11.19 We identified several such cases, which we believe might have been avoided by the existence and use of a strategic plan. A strategic plan might have meant that the operational priority given natural resource conservation (paragraphs 11.46 and 11.49), would have better reflected its importance in the Parks program mandate A strategic plan would provide direction for more efficient use of personnel (paragraph 11.80) and for managing support functions such as informatics (paragraph 11.106).

11.20 The Canadian Parks Service should develop a strategic plan and review operational plans in relation to objectives set out in the strategic plan.

Canadian Parks Service response: *The Canadian Parks Service is developing a strategic plan that will serve as a guide for setting program direction for operational plans.*

11.21 The Canadian Parks Service should use these plans as a means of determining direction, including setting priorities, allocating resources, making decisions, controlling activities and reporting to Parliament.

Canadian Parks Service response: *Current processes for the translation of the Canadian Parks Service strategic plan into program direction, the setting of priorities, the allocation of resources and the control of activities will be more formalized.*

Performance Measurement and Reporting

11.22 Management needs reliable information to assess the effectiveness with which program objectives are being achieved. The objectives are included in the program's mandate to "protect and use" (paragraph 11.7) which requires, among other things, the establishment of parks, the conservation of resources within parks, and the appropriate presentation of these resources to Canadians. A suitable mix of ongoing performance measurement and periodic evaluation is required to produce such information and report to both management and Parliament.

National Parks Systems - Opportunities to establish parks in some natural regions are diminishing

11.23 The plan for the national parks system, approved by Cabinet in 1979, calls for park representation in each of Canada's 39 defined land regions.

11.24 Program management reports that "the extent to which the parks systems include representative examples of Canada's heritage has been the prime measure of the Program's effectiveness" regarding its protection objective.

11.25 Management has developed a planning procedure which seeks to identify areas representative of each of these regions. The park planning system is well designed, with one important exception -- it lacks a schedule for completion. Once areas within natural regions are identified, the system plan does not provide guidance on which national parks should be established and in what order of priority.

11.26 At the time of our audit, 21 of the 39 land-based regions (54 percent) were represented by at least one park or reserve for a park. Of the remaining 18, 7 have proposals for the conversion of a representative area to a park (although 3 of those proposals are inactive); 7 others have areas identified but proposals have not yet been made; and 4 remain for which representative areas have not yet been identified.

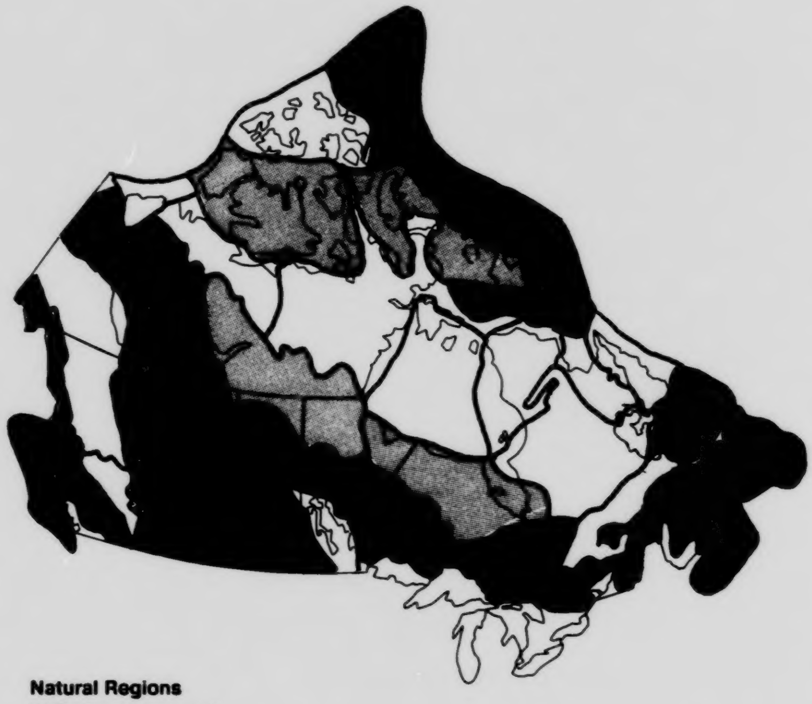
11.27 In each of the 18 natural regions not yet represented, opportunities to establish parks are diminishing. In fact it may already be too late to represent certain regions in their natural state. A recent study commissioned by the Minister of the Environment states that the same may be true within 20 years in these still unrepresented regions.

11.28 The Canadian Parks Service reports to Parliament on progress in acquiring new parks and on the number of natural regions represented. The Canadian Parks Service does not report on the likelihood of not achieving the objective of completing the parks system.

11.29 Of the 15 parks established since 1971 (when formal planning procedures were instituted), five were in natural regions already represented by one or more national parks. Of these, two new parks (Bruce Peninsula and Mingan Archipelago Reserve) were established in a region which was already represented by two parks (Georgian Bay Islands and Point Pelee). The rationale offered by CPS was that the existing parks did not sufficiently represent the diversity of the region. However, the effect of such additions is to direct resources toward improving representation in areas already represented rather than establishing parks in regions not yet represented.

Almost half of the natural regions are not yet represented.

NATIONAL PARKS' 39 NATURAL REGIONS



Natural Regions

21 Regions represented

■

18 Regions not represented

▨ 4 Regions with active park proposals

☐ 14 Regions without proposals

Exhibit 11.3

11.30 "A Plan For Completing The National Parks System" was prepared in October 1982 but was never approved by senior management. More recently, CPS advised us that in 1989-90 management expects to produce a review of the overall parks system plan. The review is intended, on a region-by-region basis, to describe the adequacy of representation of the natural regions by existing park(s). For regions not represented by a park, the current stage of planning will be identified. In each such region, the factors, including "risk to natural resources", that affect the speed of the park creation process will also be analyzed. Any other existing forms of environmental protection (e.g. provincial parks) will be identified. However, this review does not intend to project a range of completion dates for the parks system. Different levels of resource availability result in different completion dates.

11.31 The Canadian Parks Service's biennial report to Parliament should include both the progress made in completing the national parks system and an assessment of the probable completion dates for the national parks system under circumstances existing at the time of the report.

Canadian Parks Service response: *The Canadian Parks Service's report in future will include statements concerning these matters to the extent that it is possible to make such an assessment, given that many factors affecting new park establishment are beyond the control of the federal government, such as comprehensive native land claims and federal/provincial/territorial negotiations.*

Attendance statistics are still not reliable

11.32 The presentation of heritage resources to the public is part of the CPS program objective. Attendance statistics are used by program management to inform Parliament on the effectiveness of its presentation activities and to inform decision makers regarding, for example, park operation seasons, staff levels and public demand for specific services.

11.33 Prior to 1983, CPS recognized serious difficulties with the reliability of its attendance statistics. Our last audit, in 1983, highlighted the unreliability of reported numbers. It was not until 1988-89 that new procedures, which are sound in theory, were implemented in some parks.

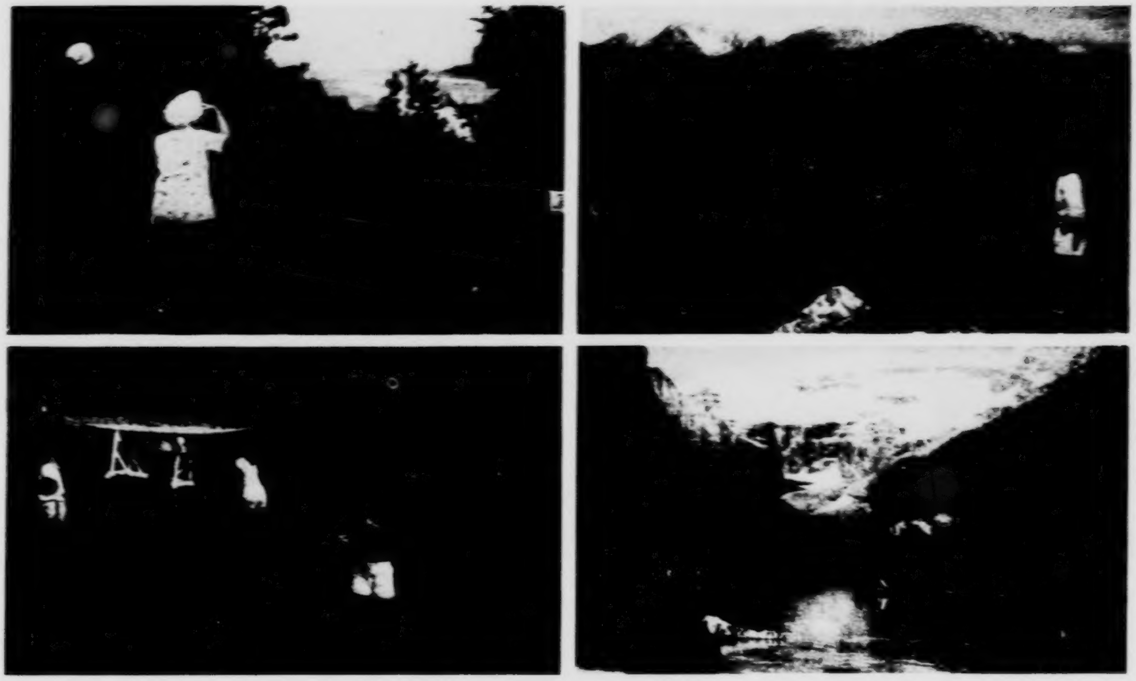
11.34 The new procedures are intended to distinguish between entrants to the parks who are simply using the roads as thoroughfares, and those who are there for heritage appreciation or recreation. The number of visits reported should be an accurate count of the latter group

11.35 The present plan is to have the new procedures fully in place for April 1993. It calls for a quality assurance review of the new procedures on a region-by-region basis. One result of this approach is that some parks that account for very significant portions of the total number of visits (e.g. Banff, Jasper, Yoho and Kootenay) will not be part of the new system until late in the process In all, more than 10 years will have passed before recognized deficiencies in data used for program management are corrected

Excessive delays in developing performance measurement information

11.36 Since 1976 Treasury Board policy has required that departments establish procedures for routinely measuring their ongoing operational performance. The Canadian Parks Service does not yet have procedures for performance measurement. Such procedures would routinely measure the ongoing performance of operations in terms of the effectiveness with which objectives are being achieved and the efficiency with which they are being administered.

11.37 In 1984, management acknowledged the need for better program performance information and initiated a Management Information Framework (MIF) project to meet the need. Some performance measurement information is expected beginning in 1991-92. However, this project is not expected to provide comprehensive systematic measurements of the results of CPS operations before March 1994 -- about 10 years after the initial decision was taken to develop and implement ongoing measures of performance.



Photos: Canadian Parks Service

Attendance statistics should present the full range of available park activities (see paragraphs 11.32 to 11.35).

Management is not conducting program evaluation

11.38 Treasury Board directives and guidelines call for the evaluation of all major components of a program about once every five years. These evaluations are intended to provide management with credible, timely, useful and objective information to be used for resource allocation, program improvement and management accountability.

11.39 A departmental program evaluation function has existed in the Department of the Environment since 1978-79. Current resources allocated to the function are three person-years and approximately $200,000. However, as of 31 March 1989, the first CPS program evaluation study had yet to be started. Two preparatory efforts to evaluate CPS operations, in 1982 and in 1985, did not lead to evaluation studies. We are told that the first full evaluation of a Parks program activity is now scheduled for 1991-92.

Protecting Natural Resources

11.40 Resource conservation is a central activity of the Parks program mandate. The Parks Program Policy includes the statement that "natural resources within national parks will be given the highest degree of protection to ensure the perpetuation of a natural environment essentially unaltered by human activity."

11.41 Each national park is required to have a Park Management Plan. An integral component of each park's plan is a Park Conservation Plan in which the park identifies and establishes priorities for its natural resource management problems. For each problem, a

Resource Management Plan is to be prepared to specify needed studies, what is to be done about the problem and how it will be monitored.

Lack of resource management plans

11.42 We observed that the Park Conservation Plans were prepared and were reviewed at the regional and national levels. However, in the majority of cases, the Resource Management Plans, which are fundamental to the process, have not been prepared and the necessary studies and monitoring of the resources have not been done.

11.43 The Canadian Parks Service should prepare and use Resource Management Plans as required and monitor and report the progress made in resolving natural resource problems.

Canadian Parks Service response: *Resource Management Plans are prepared on a priority basis. These plans require capital funding to implement and efforts are underway to obtain this funding through re-allocation of existing resources. The Natural Resource Management Process provides for monitoring and reporting on the progress made in resolving natural resource problems. This monitoring program can only be effective if additional long-term operating resources can be committed.*

Natural resources not given priority

11.44 Resource management is designed to protect selected areas of land and water and the plants and animals within those environments. It begins with the establishment of a park and continues with the protection of the resources within the park boundary

11.45 Park management is expected to establish parks which are representative of a natural region. This expectation has sometimes been prevented by commercial interests during the negotiations leading to an agreement establishing a park boundary. One example is the exclusion from Kluane National Park of caribou calving grounds in the Klutlan Glacier area and Wolverine Plateau because of existing mining interest in these areas.

11.46 The Canadian Parks Service is charged with protecting the natural resource ecosystems within each park. This objective is threatened when commitments to the development of park visitor facilities precede the development of the basic inventory of natural resources. Two examples are the proposed chairlift or funicular at an unstable site in Gros Morne National Park and visits to Ile Nue (a short grass terrain with fragile Arctic plants and fossils) in Mingan Archipelago National Park Reserve.

11.47 The Canadian Parks Service should ensure the inclusion of 'escape clauses' in park establishment agreements to allow park development plans to be changed if threats to resources are discovered after the agreements are made.

Canadian Parks Service response: *The Canadian Parks Service attempts to avoid including specific development commitments in new park agreements.*

Breaches of resource protection policy

11.48 Canadian Park Service policies are designed to conserve ecosystems. The policies ban all forms of damage or removal of resources except certain traditional activities and then only under conditions specified at the time of park establishment.

Resource Management Plans are not prepared for high priority natural resources.

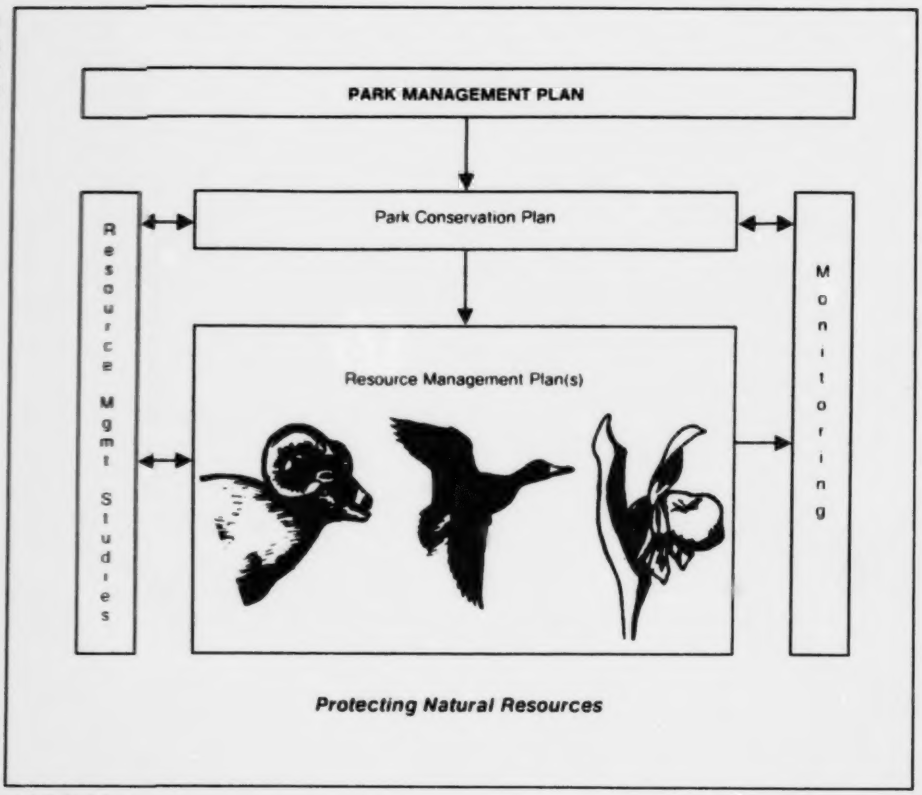


Exhibit 11.4

11.49 In practice, however, CPS has allowed many breaches of the resource protection policy. There are examples of damage to plant life (a growth of the Franklin's Lady's Slipper, a rare native orchid, was destroyed by the placement of a campsite at Pukawska National Park) and wildlife (Dall sheep were disturbed by visitor encroachment at Kluane's Sheep Mountain). Other situations include non-monitored duck hunting at Point Pelee National Park (prohibited by the Minister, June 1989), non-authorized taking of bear at Wood Buffalo National Park, and snowmobiling in non-authorized areas of Gros Morne National Park.

11.50 The Canadian Parks Service should ensure appropriate protection of natural resources consistent with its own policies.

Canadian Parks Service response: *Ensuring priority is given to the protection of natural resources requires the clear commitment of adequate fiscal and manpower resources to the planning, implementation and monitoring of established and approved plans and processes. Park plans identify key issues and the steps to be taken in their resolution. However, due to competing priorities sufficient financial and human resources are not always available.*

Protecting Physical Assets

11.51 Our audit of CPS' physical assets focussed on the management of the in-service (in use) stage. We did not examine the planning and acquisition and disposal stages of their life cycle. These assets include buildings (contemporary and historic), utilities, campgrounds, trails, roads, canals and major equipment. The replacement cost of these assets was estimated at $3.7 billion in 1988-89. In the same year CPS spent approximately $62 million on their maintenance.

11.52 At the time of our 1983 audit, CPS was at an early stage of introducing its Maintenance Management System (MMS). Currently, MMS is the main system used by CPS to standardize maintenance quality and estimate maintenance resource needs. Its primary objective is to help sites efficiently maintain their fixed assets in their as-constructed condition. The concepts underlying MMS are well established and have been proven in practice in other organizations.

Under-use of the maintenance management system is impeding efficiency improvement

11.53 The Canadian Parks Service uses MMS in a way that obscures its primary objective. The full potential of MMS is not being realized because its use is oriented toward budget justification and spending accountability but not toward improving the efficiency of maintenance functions.

11.54 Few system-wide reviews of maintenance functions have been conducted. This has made it difficult to refine standards and improve the data base supporting MMS. Measures of system-wide performance for specific maintenance functions (e.g. grass cutting) are not generally available in CPS. Detailed performance results are not summarized and analyzed in any meaningful way.

11.55 Some sites have improved the performance of specific maintenance functions. Even at the site level, however, it is difficult to determine whether a site has improved its overall maintenance efficiency. Also, management has not used successful MMS experiences at some sites to encourage efficiency improvements at other sites

11.56 Efforts to improve maintenance methods are not concentrated and co-ordinated. Except for the maintenance of vehicles and mobile equipment, regional headquarters generally do not devote resources to monitoring and improving the performance of maintenance functions at sites.

11.57 The Canadian Parks Service should develop within MMS the capability to monitor the efficiency of sites and maintenance functions.

Canadian Parks Service response: *The capability to monitor the efficiency of sites and maintenance functions through performance reporting and analysis will be reviewed and, where feasible, improved.*

Inability to review and assess the relationship between asset performance and level of maintenance

11.58 The performance of an asset is affected by a number of factors, including its design, how it is used, its level of maintenance, and climatic conditions. Historical information on these factors is not compiled by CPS in a way that facilitates review and understanding of the relationship between asset performance and level of maintenance. As a consequence, CPS lacks essential data to support life-cycle cost management of its assets.

11.59 The Canadian Parks Service should compile relevant summary data pertaining to asset performance in a manner suitable for periodic review and evaluation of maintenance policy and practice.

Canadian Parks Service response: *With the increased emphasis on performance reporting it will be possible to retrieve asset information relating to the cost of maintenance per year and the history of maintenance work performed by year.*

Overestimation of maintenance resource needs

11.60 The Canadian Parks Service uses MMS, with its asset inventory and national maintenance standards, to forecast aggregate maintenance resource needs. Total funding needs generated this way are 20 to 25 percent higher than funds allocated by Treasury Board. For 1988-89 the difference was about $17 million. Senior management feels that the levels of expenditure on maintenance activities have not kept pace with the needs of the asset base. Inadequate maintenance is one factor which may cause an asset to deteriorate more quickly than normal. The relationship, however, between an asset's maintenance history, its physical condition and its rehabilitation requirements is difficult to quantify.

11.61 We looked for, but did not find, sufficient evidence to conclude that the level of maintenance spending has led to premature deterioration of assets. We observed some assets that were in disrepair, but in most of these cases maintenance was being withheld because these assets were at the end of their working lives. The current condition of the assets we observed (confirmed by a consultant's report commissioned by CPS) suggests that current maintenance expenditure levels are within the appropriate range.

11.62 The structure and use of the current MMS overestimates maintenance resource needs. The national condition standards for certain assets are higher than needed at some sites. Also, some sites consistently exceed the national productivity standards for certain maintenance functions.

11.63 The Canadian Parks service should:

- **require sites to base their maintenance funding needs on their own proven performance data; and**
- **instruct sites to support requested changes in maintenance funding levels from prior years with explicit references to site programs and specific assets, and to describe the expected consequences of not receiving the amounts requested.**

Canadian Parks Service response: *As part of the operational planning exercise, site managers will be required to calculate their maintenance resource needs by using the maintenance standards in line with their local conditions and past experience.*

For all requests for additional funding, site managers will be required to identify the asset or facility on which work is to be performed and its replacement value, to provide a description of the work to be performed, with an accurate estimate of the cost, and the impact of not performing the work.

Potential problems in recapitalization funding

11.64 Recapitalization is the rehabilitation or replacement of an asset or major component of an asset to achieve an acceptable service condition without changing its basic function or capacity. The distinction between maintenance spending and recapitalization spending is not well defined in CPS.

11.65 There are some preliminary indications, based on a consultant's study done for CPS in 1987, that the level of recapitalization funding could become a problem in the future. The study points out that this is particularly true for roads and bridges because many have reached the point in their life-cycle where major rehabilitation work is required. We feel that these potential problems can only be addressed by considering each asset's recapitalization needs in terms of its maintenance history and intended use.

11.66 The Canadian Parks Service should:

- **base short-term recapitalization funding projections on individual asset requirements identified by site; and**

- **clarify the distinction between items of maintenance and recapitalization spending.**

Canadian Parks Service response: *Through its Project Initiation and Planning System, the Canadian Parks Service, has for some time, based short term recapitalization funding needs on individual asset requirements, by site. However, due to insufficient capital resources all of the "high" priority recapitalization projects have not been addressed.*

As part of the comprehensive review of maintenance standards the distinction between maintenance and recapitalization spending will be clarified.

11.67 At the time of our audit CPS was considering the development of an Assets Management Process (AMP) in place of the Assets Management Information System (AMIS). AMP is intended to provide information for managing assets throughout their complete life cycle by employing an improved MMS with a yet-to-be-developed recapitalization management process.

Managing the Efficient Use of Human Resources

11.68 This project dealt with the efficiency achieved by CPS in the use of part of its labour force. It focussed on:

- the extent to which service quality had been maintained during a period of resource constraint; and

- the extent to which CPS minimizes organizational layering, overhead and administrative burdens and redundancy.

11.69 For 1988-89 CPS had 4,678 authorized person-years, including seasonal staff, to meet the requirements of a reported 28 million visitors annually. The approximate person-year distribution was as follows: 11 percent at Headquarters, 17 percent in regional offices, and 72 percent at the field level (including district offices, parks and sites).

11.70 The total of person-years used by CPS in 1987-88 was relatively unchanged from our audit five years earlier. However, factors existed that placed the organization under resource constraint during the intervening years. Two of the primary factors were:

- operation and maintenance budgets, in 1984-85 dollars, did not change significantly; and

- during this period CPS added five new national parks to the system.

11.71 Our audit focussed on the following components of CPS:

- Visitor Services and Interpretation functions in both National Parks and National Historic Parks and Sites;

- Finance and Administration; and
- National Historic Parks and Sites Headquarters functions.

11.72 Visitor Services and Interpretation. The Visitor Services and Interpretation activities exist at all three levels of the organization (Headquarters, regions and sites) for both natural and historic parks. In some instances these functions have been grouped under a single heading: Visitor Activities. In 1987-88, about 922 Visitor Activities person-years comprised approximately 20 percent of CPS' total person-years.

11.73 Interpretation involves education programs designed to increase visitor appreciation and enjoyment of Canada's heritage resources. The activity is delivered through park or site interpreters and non-personal interpretation projects such as automated audio-visual programs, radio presentations, exhibits, signs or publications and messages to the general public. Visitor Services involves the provision of direct services to the public, including park gate attendants, campground attendants, lifeguards at swimming pools, and counter staff at information centres.

Lack of adequate information to efficiently manage visitor services activities

11.74 As identified in our 1983 audit, CPS did not have the information base needed to support the efficient management of Visitor Services activities. Although a number of initiatives were in progress, these are not yet providing regular efficiency and productivity reports for management.

11.75 Two examples of initiatives intended, ultimately, to improve the quality of information available relating to visitor services are the Visitor Activities Management Process (VAMP), and the Management Information Framework (MIF). Neither system is yet fully developed. Without appropriate information it is difficult for CPS to assess the efficiency of the Visitor Services and Interpretation Activity.

Decline in service is linked to resource constraints

11.76 The Canadian Parks Service has operated for a number of years under conditions of resource constraint. In the three-year period prior to 1983-84, CPS reduced its strength by approximately 200 person-years. Since then, total person-years have remained relatively constant while management of the program has expanded through the addition of five new parks.

11.77 The Canadian Parks Service has no comprehensive measure of visitor satisfaction. Therefore, the impact of this program expansion on the quality of visitor experiences is not well measured. Nonetheless, reports of comments made during public sessions and letters from the public point to a decline in service. Comments by CPS management in planning documents, and other information sources, also indicate a decline in the quality and extent of service being provided. This apparent decline is often linked by CPS to the reduction in person-year resources.

11.78 Where CPS is required to make resourcing decisions which will reduce the quality and level of service, management must be in a position to estimate the subsequent impact on park visitors. We do not believe management is receiving the information needed to assess these impacts.

11.79 The Canadian Parks Service should implement information systems that provide measures of service quality and visitor satisfaction. This information should be used as input to resource allocation decisions.

Canadian Parks Service response: *The Canadian Parks Service has recognized this need and is developing performance indicators for service quality and visitor satisfaction which will be used in making resource allocation decisions.*

Opportunities to increase efficiency

11.80 We believe that there are opportunities to reduce person-years in overhead and support functions that will not have a direct impact on service quality and availability. These opportunities could include combining Visitor Services and Interpretation units at regions and sites. Also, CPS could determine whether alternative staffing methods would be appropriate for certain permanent positions within parks that essentially receive most of their visitors during the peak summer period. We recognize that there may be a need for some positions on a year-round basis.

11.81 Future resource reallocation initiatives should pay appropriate attention to opportunities to reduce the person-years involved in indirect and overhead functions and their reallocation to operational areas.

Canadian Parks Service response: *Initiatives in this regard have begun with the result that the former separate positions of Chief, Interpretation and Chief, Visitor Services have been combined and reclassified in four regional offices and in several national parks. Reductions to our overhead costs (though not person-years) may be available through proposed changes to the service agreement between the Canadian Parks Service and the Canadian Government Exhibition and Audio-Visual Centre.*

11.82 Finance and Administration. The Finance and Administration function is responsible for the following comptrollership activities at all three levels of the organization: finance; administration; contracts; materiel management; program planning; and informatics. The DOE Corporate Finance and Administration organization represents a fourth level. Functional leadership is provided from CPS Headquarters to the regional offices and to the field. A total of 691 person-years (14 percent of total CPS person-years) were involved in this function in 1987-88.

11.83 Our audit approach in this organizational component was to determine whether conditions in CPS are such that methodologies used in both the private and public sector to identify productivity improvements and savings opportunities in support organizations could be applied. Typically, the application of these methodologies, which include workload measurement, organizational streamlining, practice and procedure rationalization and simplification can result in savings opportunities of about 10 to 20 percent of person-years and the related payroll costs.

11.84 Our review of CPS Finance and Administration indicates that a potential for savings exists for the following reasons:

- Since 1983-84, total person-years used by these functions have remained relatively constant at 691, or 14 percent of CPS resources in 1987-88.
- In 1987-88 Finance and Administration person-years, as a proportion of total regional staff (including regional headquarters, districts, areas and sites), varied across the regions from 11.9 percent to 15.1 percent.
- There are permanent year-round Finance and Administration positions at some parks which receive most of their visitors during the peak summer period.

- Organizations are characterized by small operational units. At the regional offices we visited, the average number of staff for which each supervisor was responsible was 3.5.

- In the Ontario regional office, a recent assessment of Finance and Administration processes and practices, including workload measures, identified opportunities for reallocating person-years from accounting operations, contracting and word processing to other areas. These improvement opportunities were within the range previously noted in paragraph 11.83.

- In the past five years there have been significant increases in the use of computer technology within these functions.

11.85 Taken together, we believe these points indicate that opportunities exist to streamline and consolidate Finance and Administration organizations, and to match resources more appropriately to workload and service requirements, thereby improving productivity.

11.86 We believe these opportunities could be realized primarily through reorganization, improved methods and procedures, elimination of unnecessary tasks, modified service levels and resource planning based on workload measurement.

11.87 To ensure that any changes take into consideration the sensitivities of everyone affected, and that ideas and opportunities for improvement are fully identified and explored, managers and staff at all levels should be involved in any initiatives undertaken in this area.

11.88 The Canadian Parks Service should undertake a comprehensive assessment of improvement opportunities within Finance and Administration that would involve all levels of staff and ensure that employee sensitivities are considered.

Canadian Parks Service response: *Much work has been done in this area over the past few years and will continue.*

11.89 National Historic Parks and Sites. The National Historic Parks and Sites (NHPS) Directorate is located at Headquarters. It provides functional leadership to the regions and field operations. It also provides direct services that are separate from the field operations. For example, the Architectural History Branch is responsible for implementing the Act for the Protection of Heritage Railway Stations (Bill C-205, 1988). It has also been assigned responsibilities associated with Canada's signing of the World Heritage Convention. About 205 person-years are allocated to the NHPS Directorate at Headquarters; this allocation represents a decrease from 1983-84 of 33 person-years (14 percent).

Improvements in project management and functional leadership

11.90 Since our 1983 audit, progress has been made in the areas of project management, functional leadership and co-ordination with policy directives. For example, the process for allocating resources to research projects in the Archaeological Research Branch considers the priority assigned to each project. Also, the responsibilities of functional managers are now defined and communicated more appropriately. Initiatives have been taken to co-ordinate policy with the National Parks Directorate For instance, policy planning and direction on co-operating associations have been combined.

11.91 In our opinion, NHPS Directorate has made identifiable progress toward improved organizational efficiency and effectiveness since 1983.

Managing Revenue and Cost Recovery

There is little incentive to increase fee revenues

11.92 In 1988-89 CPS generated $37.7 million in revenues as follows:

	(millions of dollars)
Entrance fees	7.9
Visitor services (camping, swimming, etc.)	11.4
Land lease and concessions	12.4
Other	6.0
	37.7

11.93 CPS states it has little incentive to seek innovative means to augment existing revenues or generate new sources. All revenues accrue to the Consolidated Revenue Fund, but CPS must absorb the costs of initiating and implementing revenue generating activities. At the time of our audit CPS was examining with the Treasury Board various ways to solve this dilemma.

Foregone revenues

11.94 The Canadian Parks Service has indicated that the time required to get fee changes through the approval process can be as long as 18 months. This restricts management's ability to react quickly to market conditions. The fee approval process requires extensive reviews and approvals within and outside CPS. At the time of our audit there was no formal tracking system to monitor progress and warn senior management of delays in the approval process. The Canadian Parks Service estimates that foregone revenues resulting from delays in the approval of fee changes were $700,000 for 1988-89.

11.95 The Canadian Parks Service should implement a monitoring system for the fee approval process and, in so far as it has control over the process, take corrective action to ensure that fee changes are approved on a timely basis.

Canadian Parks Service response: *The Canadian Parks Service has no control over major components of the regulatory process and therefore cannot react directly to observed delays in all cases. However, the Canadian Parks Service will implement a monitoring system for the fee approval process, with a view to reducing internal delays. In addition, representations will be made to the central agencies involved in driving the process to ensure that timely corrective measures are applied whenever the tracking system warns of delays.*

Opportunities exist to increase revenues

11.96 Entrance fees to national parks have not changed since 1986-87, and no fee increases are proposed for the 1989-90 season. Similarly, entrance fees to national historic parks have not been changed since 1985-86. However, fee changes are proposed for two historic parks for the 1989-90 season.

11.97 Entrance fees are charged at only five national historic parks. In 1987-88 there were at least six others, each of which reported more than 100,000 visits, for which there were no entrance fees. Five of these six were included in a 1985 internal report, "Entry Fees for National Historic Parks and Sites", which identified nine additional historic parks as prime candidates for the introduction of entrance fees. Since that time only one of the nine has implemented fees. To take a broader view, entrance fees for 25 historic parks were discussed at a 1987 Program Management Committee meeting, and a decision to levy fees was delayed pending Treasury Board approval of some form of revenue sharing. The Canadian Parks Service is currently preparing a proposal on the possibility of introducing entrance fees at more historic sites in 1991.

11.98 The Canadian Parks Service should ensure that fees are charged at all sites where it is appropriate to do so.

Canadian Parks Service response: *A process has been developed and approved to ensure that user fees will be introduced at all national historic sites where it is appropriate to do so.*

The costs of all townsite services are not recovered

11.99 Our 1983 audit observed that CPS did not have adequate accounting systems in place to support full cost recovery for specific services provided. This has now been remedied.

Improvements in some management planning and control systems are needed to increase economy and efficiency of operations and to ensure that both management and Parliament have adequate information on results.

11.100 The Canadian Parks Service charges residents of townsites within the national parks for sewage, water, garbage and street works services. However, other services -- such as fire protection, recreation and bylaw enforcement -- are provided without specific charges to residents.

11.101 The Canadian Parks Service should implement cost recovery for townsite services such as fire protection, recreation and bylaw enforcement which are not currently subject to specific charges.

Canadian Parks Service response: *The Canadian Parks Service will review the feasibility of implementing cost recovery for these services; however, the current National Parks Act does not provide the necessary legislative authority.*

Billing errors due to poor internal controls

11.102 Although the billings process was not part of our audit scope, we noted a case where billings were understated by $170,000. As a result the Canadian Parks Service initiated an audit and identified an additional $322,000 in understated billings. The Service has billed for these amounts and we have been informed that only $151,000 remains unpaid.

Managing Informatics

Speedy deployment of office automation technology

11.103 Before 1983, CPS was relatively unsophisticated in its use of computer technology. Data processing activities were restricted to systems which had been in operation since CPS joined DOE in 1979.

11.104 The Canadian Parks Service became involved in the Department of Communications' Office Communications Systems program in 1983. Now its major focus for informatics is the Departmental Office Technology System (DOTS). This initiative is in the last year of a $16 million, four-year program that will see 1,200 DOTS terminals installed across the country. This will provide access to standard office automation functions such as electronic mail, word processing, spreadsheets and, eventually, to local, regional and national data bases.

11.105 In our opinion, the most significant benefits -- justifying current expenditures -- will be obtained when local, regional and national applications are installed. An internal study is under way to determine the total additional office automation and application needs.

Lack of a long-range informatics strategy and problems in project management

11.106 Major informatics initiatives, involving expenditures of at least $24 million over a four-year period from 1985, have been developed without a long-range informatics strategy or plan. A long-range plan would have defined a technology strategy and specified how it would support program objectives and management and user information needs. It would have provided a better foundation for the development of major systems. It could also have reduced project development and management problems such as those encountered in CPS' Management Information Framework (MIF) and Asset Management Information System (AMIS) projects, both of which will suffer from extensive time overruns from original schedules. For example, the estimated date for completion of MIF, which was started in 1985, was to be 1989 and is now scheduled for 1992-93. There was no scheduled completion date for AMIS (now the Assets Management Process, AMP) at the time of our audit.

11.107 The Canadian Parks Service should develop and implement a plan for a long-range informatics strategy. This should fully define the projected direction for informatics, as well as objectives and priorities over a five-year period.

Canadian Parks Service response: *The informatics strategy/long-range plan is being developed. It will provide a longer focus than the current annual planning.*

Information for Parliament

Inadequate information for Parliament and management

11.108 We believe that Part III of the 1988-89 Estimates for the Parks program presents a satisfactory picture of the program's expenditure plans. However, results information is insufficient because CPS' systems are not adequate to provide reliable program performance information to management or to Parliament. Parliament is therefore hampered in its ability to effectively review program expenditures.

12

DEPARTMENT OF EXTERNAL AFFAIRS

Consular Services

12

DEPARTMENT OF EXTERNAL AFFAIRS

Consular Services

Main Points

12.1 The Department of External Affairs provides protection and assistance to Canadians who live and travel abroad. The Department reports that Canadian missions abroad extended services to Canadian citizens on over 600,000 occasions in 1988 ranging from routine inquiries to situations involving illness, accident and death (paragraph 12.3).

12.2 In general, the Department of External Affairs' consular officers and staff provide these services in a dedicated way. We have identified a number of areas in the management process that, in our view, can be improved, which would enable the Department to better meet increasing demands for service in an environment of restraint (12.11):

- The Department has not defined the range and extent of services to be provided in precise enough terms to ensure treatment of Canadians that is consistent and is perceived as fair and that also ensures the most effective use of resources at each post (12.16 to 12.27).
- The Department's current deployment and training procedures do not provide assurance that officers with the appropriate experience and training are placed at posts where consular work is the most difficult (12.28 to 12.38).
- The Department has not fully exploited the potential of its public awareness program for informing Canadians who travel abroad about potential dangers and about what services are, and are not, available abroad (12.39 to 12.44).
- The use of honorary consuls is a less expensive way of providing certain services than establishing a regular mission. However, the Department has not clearly defined their consular responsibilities and does not adequately supervise their delivery of services (12.45 to 12.50).
- The Department has not developed and kept up-to-date contingency plans for foreign crisis situations at all its medium-to-high risk posts (12.55 to 12.57).

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DEPARTMENT OF EXTERNAL AFFAIRS

Consular Services

Introduction

12.3 Consular services aim to assist Canadians outside Canada. The objective of consular services is to protect the interests of Canadians living and travelling abroad. The Department of External Affairs provides a wide range of services to help Canadian citizens outside Canada deal with problems where official assistance is required. Among these are issuing passports, notarizing documents, arranging for the transfer of funds to the destitute, helping the incapacitated return to Canada, ensuring that those detained or imprisoned abroad are treated fairly under local laws, and assisting with citizenship registration applications.

12.4 Services are a joint responsibility. Consular services are provided by External Affairs through the Canadian Interests Abroad Program. They are the joint responsibility of the Consular and Immigration Affairs Bureau at headquarters and 105 posts abroad. Headquarters provides functional guidance to the posts on specific cases, develops guidelines, liaises with other government departments as necessary, and is responsible for training and the public awareness program. The delivery of consular services is carried out by consular officers and local staff at the posts and a growing number of honorary consuls, under the responsibility of heads of missions. The terms 'post' or 'mission' are used to refer to Canadian embassies, high commissions, consulates-general and consulates.

12.5 Direct costs are estimated at $14 million annually. The Department estimates the cost for these services, excluding headquarters overheads, at $14 million a year. The Department allocated 77 Canada-based person-years to the provision of consular services in 1988-89. To assist officers abroad, posts used locally-engaged staff for an equivalent of about 120 person-years. Over the past two years, the number of Canada-based person-years assigned from Ottawa to consular services abroad has decreased by almost 13 percent while the number assigned to trade, immigration, political relations and economic relations has remained virtually unchanged.

12.6 Program delivery environment is diverse. Service delivery is governed by international law, the social environment of each country, the number of Canadians living and travelling abroad, the number of Canadians of plural nationality, the demand for service by Canadians around the world, and the competition for resources within the Canadian Interests Abroad Program. A multilateral treaty, the Vienna Convention on Consular Relations, makes it possible for Canada and the other 150 signatories to assist their nationals abroad while respecting the sovereignty of other countries.

12.7 The needs of Canadians abroad and the demands placed on consular services within a country vary with the social and cultural differences between that country and Canada. Thus, the mix and amount of consular services can vary significantly from one post to another. For example, in some countries, prisoners get insufficient food because prison officials expect prisoners' families to supplement rations. Embassies must, therefore, arrange for food to be delivered to Canadian prisoners in these countries.

12.8 Many more Canadians are living and travelling abroad. Another important factor affecting the demand for consular services is the growing number of Canadians travelling or living abroad. The Department reports that in 1987 Canadians made 2.6 million trips to countries other than the United States, compared to 1.8 million trips in 1977. There

The consular staff at Canada's missions abroad provide services to Canadians such as issuing passports and assisting Canadians detained in foreign prisons (see paragraphs 12.3 and 12.58).

are almost five million valid Canadian passports in circulation, an increase of 40 percent during the past five years. In 1982, the Department estimated that 1.5 million Canadians resided outside the country. In 1987, the Department reported that this estimate had risen to 3.0 million. Although their actual number is unknown, dual or plural nationals represent an important and growing percentage of these non-resident Canadians.

12.9 New patterns of international trade, tourism and development activities have drawn Canadians to previously remote corners of the world. Because these patterns create a demand for consular services worldwide, and because resources are constrained, the Department has supplemented its network of posts with 48 honorary consuls and a reciprocal consular agreement with Australia. The United Kingdom continues to provide some services to Canadians in certain localities where Canada is not officially represented.

12.10 Competing demands for consuls' time. Officers assigned to consular work abroad are usually required to do other departmental work; political and economic reporting, public affairs and cultural activities, or immigration work can often take precedence over consular duties. In addition, Foreign Service Officers are assigned to posts on a rotational basis, for a period of two to four years.

12.11 Consular work is demanding and varied, requiring well developed interpersonal skills and quick responses to complex situations. As well as helping Canadians in difficulty meet their physical and emotional needs, consuls and their staff must also handle, with tact and courtesy, demands for service that may be unreasonable or unrealistic. Canadians travelling or living abroad, and their families in Canada, often expect the Department to resolve any problems they encounter. Some consular cases become the object of intense media and political scrutiny and put considerable strain on already scarce resources. (See Exhibit 12.1)

Audit Scope

12.12 We looked at the overall management of the consular activity, examining how the Department delivers consular services and how headquarters directs the posts as to the range and extent of services to offer. We assessed the mechanisms for ensuring that consular personnel assigned to difficult consular positions abroad had the appropriate experience and training. We also examined the public awareness program for consular services and the responsibilities and monitoring of honorary consuls.

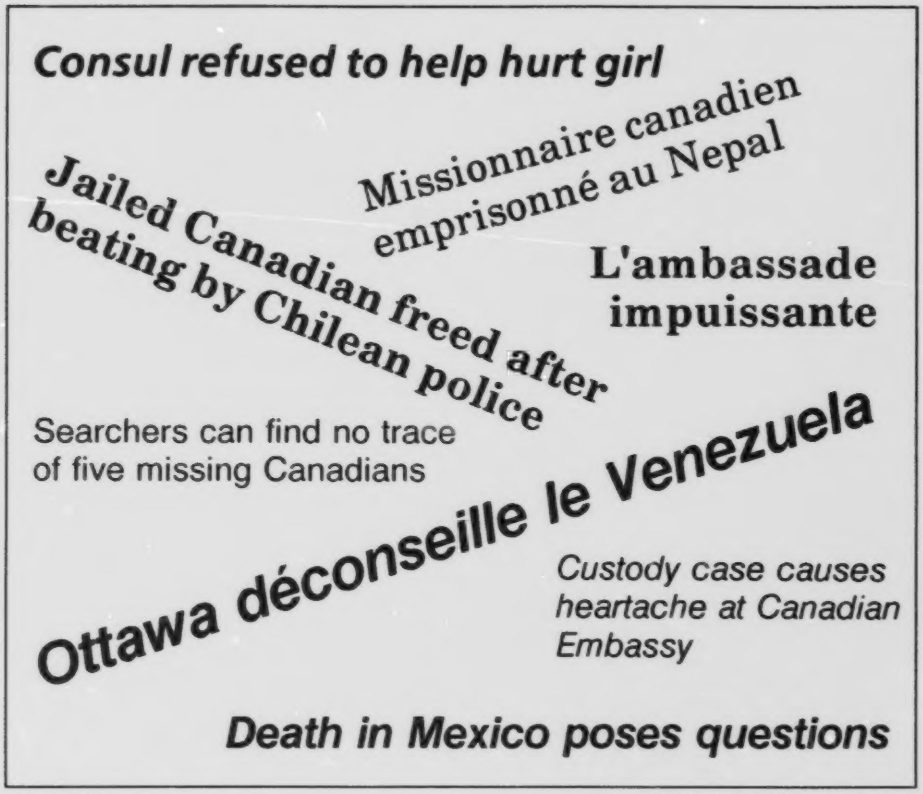
Our audit objective was to examine how the Department of External Affairs manages the delivery of consular services to Canadians living or travelling abroad.

12.13 We assessed how the responsibilities of consular services for contingency planning were carried out. We did not review the Department's management of actual foreign crises, nor did we assess the feasibility of the contingency plans. We examined the procedures for issuing passports at the posts. Our scope did not include an examination of the Passport Bureau or the issuance of passports in Canada.

12.14 We conducted our audit at External Affairs headquarters in Ottawa and at selected posts abroad. For comparative purposes, we reviewed policy direction to consular officers of three other countries whose attitudes toward their responsibilities to their citizens are reasonably similar to our own.

12.15 The Department had not done any internal audits in the areas within our audit scope or measured the effectiveness of consular activities during the past five years. A program evaluation of consular services was, however, under way in 1988-89. Although the results had not been documented, we were informed by the Department that its preliminary conclusions were consistent with ours.

Some consular cases become the object of intense media scrutiny.



Consul refused to help hurt girl

Missionnaire canadien emprisonné au Nepal

Jailed Canadian freed after beating by Chilean police

L'ambassade impuissante

Searchers can find no trace of five missing Canadians

Ottawa déconseille le Venezuela

Custody case causes heartache at Canadian Embassy

Death in Mexico poses questions

Exhibit 12.1

Observations and Recommendations

The Range and Extent of Consular Services: A Need for More Specific Definition

12.16 The Department of External Affairs has developed consular guidelines which, in general terms, identify the protection and assistance services that its staff may provide to Canadians abroad. These guidelines, contained in a manual, are designed to give consular staff the flexibility to adapt departmental services to local conditions. The Department relies on the judgment of consular staff in interpreting these general guidelines to respond appropriately to the needs of Canadians in difficulty.

12.17 The Department, however, has not defined the range and extent of services to be provided in precise enough terms to ensure consistent treatment of Canadians that is perceived as fair, that provides for proper accountability, and that also ensures most effective use of resources at each post.

12.18 The need for consular services varies in number and complexity from country to country, there is continual rotation of personnel among dissimilar posts, and consular officers are assigned to many other responsibilities. Therefore, we expected that the Department would provide guidance to its consular staff at the missions by tailoring the range or types of services to be provided, and the extent or amount of each service, to the conditions at each post. We expected that each post would have a clear specification of

Consular staff at a mission abroad assist a young Canadian traveller who was robbed of his possessions (see paragraph 12.11).

the type and amount of service that were obligatory and the type and amount that were discretionary. For example, it would be useful to determine, by country, whether consular staff must visit Canadians detained by local authorities, how often they should visit imprisoned Canadians and what specific action must be taken when a Canadian is reported missing.

12.19 We recognize the need for some flexibility and discretion at missions. However, with only a general description of the range and extent of services to guide its consular staff, there is a risk that they will provide unnecessary services and neglect those that are needed, or that they will do too little or too much in individual cases. Complete reliance on the individual judgment of consular staff in interpreting the manual heightens the risk of inconsistent treatment of Canadians or treatment that is perceived as unfair. At present, consular staff decide on a case-by-case basis how much, if any, service should be provided.

12.20 Inconsistencies in services provided at posts. Our visits abroad confirmed that some services may not be appropriate for the posts to provide. For example, some missions provide assistance in private legal matters such as real estate transactions and lawsuits. Others were involved in returning purchases by tourists to vendors and translating private documents. Some missions act as a forwarding address for mail for Canadian travellers while others help tourists with their travel plans.

12.21 Our visits also confirmed that there were inexplicable variations among posts in the amount of service provided. For example, Canadians imprisoned in one country where conditions are viewed as good by the Department are visited once a month while those in another whose prisons are viewed as considerably harsher, and where Canadian prisoners have been allegedly abused by authorities, are visited once every 3 to 12 months. Similarly, posts have not established target delivery times for issuing passports. At one post that we visited, it took an average of one week to issue a passport while at another it took six weeks.

12.22 The case studies in Exhibits 12.2 and 12.3 illustrate how complete discretion in interpreting consular guidelines can lead to inconsistent or unfair treatment. These cases occurred during the past three years.

TWO VERY DIFFERENT RESPONSES TO INDIVIDUALS ASKING FOR HELP

The Department allows consular staff considerable discretion in interpreting guidelines when deciding how much help to provide Canadians in trouble. Case 1 is a situation where a Canadian in need of a medical evacuation was not helped at all. Case 2 shows how consular personnel did arrange a medical evacuation back to Canada.

Case 1

While on holiday with her family in a relatively remote region of a European country, a Canadian girl broke a leg when struck by a car. Two days after being admitted to the local hospital, the girl developed gangrene. Hospital officials informed the father that a medical evacuation to Canada might be required. He contacted the only airline that flew to that region and was told that an evacuation could not be accommodated. He then contacted the Canadian embassy. Consular staff informed him that it was not the responsibility of the embassy to help arrange medical evacuations.

Two weeks later, the girl's left foot and part of her calf were amputated.

Case 2

Authorities in a European country released a Canadian man from prison where he had served two years for drug trafficking. Using money loaned by the Canadian embassy, the man travelled to a second European country where, disoriented and agitated, he asked Canadian consular officials to repatriate him to Canada. Consular staff confirmed with local medical authorities that he was suffering from chronic hepatitis and bronchitis as well as an addiction to heroin.

While the man received local medical attention, consular staff requested and obtained Ottawa's approval for his medical evacuation to Canada. Consular staff in Ottawa made the necessary arrangements for the man to be admitted to hospital upon his arrival in Canada. Two weeks later, he was evacuated.

Exhibit 12.2

12.23 Improved accountability and decision-making. Besides ensuring more consistent and fairer treatment, mission-specific definitions of the range and extent of service would provide additional benefits. These include greater accountability, improved decision-making on allocation of resources and better ability to assess alternative delivery mechanisms.

12.24 A better definition of the range and extent of each of the consular services would also enable the Department to state the results it expected in more specific terms. This could provide a better basis for planning, assigning priorities and controlling service delivery at each post. It would also enhance measurement and monitoring by headquarters of consular services provided at posts. Only one post that we visited had a priority system

ANOTHER EXAMPLE OF TWO DIFFERENT RESPONSES TO CANADIANS IN NEED

The Department relies on its consular staff to decide when to help a Canadian in trouble abroad, based on their interpretation of the consular guidelines. Case 3 is a situation where they decided that no help was needed. In Case 4, consular staff decided that a Canadian family needed considerable assistance.

Case 3

Recently, local authorities in a European country informed the Canadian embassy that they had discovered an elderly Canadian woman with apparent psychiatric problems wandering through the international airport. She had been there for three days. She had no money and no return ticket to Canada. The authorities had admitted her to a convalescent home and asked the embassy to take responsibility for her. The embassy asked Ottawa for permission to repatriate her because of destitution.

Consular staff in Ottawa, however, refused the repatriation request and forbade the post to spend any public funds on her behalf. They concluded that she was not destitute since she received a monthly pension of $800. They decided that because she had sold all her possessions in Canada and was originally an immigrant from the European country, she was the responsibility of foreign, not Canadian authorities. Despite her desire to return to Canada and the fact that she had not been a citizen of the European country for almost 40 years, Ottawa refused to help her.

Case 4

A few years ago, a Canadian family visited relatives in a remote region of an African country. Due to the illness of several relatives, the family stayed several months longer than intended and their landlord in Canada sold their household possessions to pay for rent in arrears. During this period, the husband's business failed and he returned to Canada to recover their possessions. A year and a half later, he asked the Department of External Affairs to help repatriate his wife and five children.

The consul from the nearest Canadian embassy travelled to the remote village where the woman and her children were staying. Concerned over the health and well-being of the children, the consul recommended to Ottawa that they be repatriated and Ottawa agreed. A second trip was made to the village to collect the family and bring them to the airport. Two years after they left for Africa, the family arrived back in Canada.

Exhibit 12.3

for the delivery of services, and this had been established by the consul on his own initiative.

12.25 More clarity and specificity in the range and extent of services to be provided would enable the Department to better assess current and future demand and to plan how to use its resources most effectively to meet this demand in an environment of restraint. It would also provide the Department with a better basis for making decisions on alternative delivery mechanisms such as the cost-effectiveness of honorary consuls, reciprocal consular agreements with other countries, and fees for consular services.

12.26 While the Department has a number of mechanisms in place for managing consular services, these do not provide a satisfactory analytical basis for decisions on the right amount of resources to use, or on their distribution and location around the world. Our review of the Department's Consular Operations Management Information System revealed that it allows duplication, with the result that the actual number of consular cases and services dealt with by the Department may be significantly less than the number reported.

12.27 The Department should specify for each post the range and extent of the consular services that it will provide. It should determine, in response to local conditions, what type and amount of service are obligatory and what type and amount are discretionary.

Department's response: *Agreed. The Manual of Consular Instructions and existing policy documents provide the general guidelines and framework to those performing consular functions at headquarters and abroad. To accommodate local conditions, missions abroad will be requested to better define through the annual mission planning exercise the range and extent of services to be provided.*

Deployment and Training of Consular Personnel

12.28 The Department stresses the importance of individual judgment and common sense when consular personnel are called on to exercise discretion. Provision of consular services, nonetheless, requires experience and special skills, for instance when a consular officer reviews documentation for passport and citizenship applications or assists the next-of-kin of a deceased person.

12.29 It is therefore important that the Department assess carefully the experience, skills and other requirements of consular positions and match these with appropriately experienced and trained staff.

12.30 The Department's current deployment and training procedures do not ensure that officers with the appropriate experience and training are placed in key consular positions at the posts.

12.31 Lack of appropriate experience and skills. To test deployment and training, we asked the Department to identify the 12 posts where consular work was the most difficult. We expected to find experienced and trained officers managing consular services at these missions. Our analysis, however, revealed that 6 of the 12 officers in charge had no previous experience in consular work; in fact, 4 were on their first posting abroad. Moreover, half of them had not received the consular training course offered by the Department. Although many of the inexperienced officers were supported by experienced local staff or Foreign Service Officers with other responsibilities, we believe that an improvement in the Department's deployment practices is required.

12.32 Consular work is normally assigned to officers in the political/economic career stream of the Foreign Service. Our examination of deployment at these 12 posts suggests that this stream is not providing a steady and reliable supply of appropriately experienced and trained officers for these particularly difficult jobs. This appears to be partly due to the view within the Department that consular work is unrewarding. In a highly competitive service, where excellence in political and economic work is particularly prized and rewarded, there is not considered to be a clear path to advancement through consular assignments.

12.33 The perpetuation of this situation could impair the quality of services to the public, accentuate differences in levels of service between posts and harm employee motivation and morale. In the long run, the quality of the Department's consular services is likely to suffer, along with its reputation, if it does not provide better career opportunities for personnel doing this sort of work and if it does not increase the prominence of consular services within the Department.

12.34 The Department has recognized this problem for many years, and several studies have addressed the need to deploy personnel who are experienced in, and committed to, consular work. As yet, no significant action has been taken.

12.35 **Need to improve training.** The consular training course is aimed at anyone who will be assigned to consular work, whether only occasionally or on a full-time basis. It covers legislation and international agreements, passports, citizenship and assistance to Canadians, and also touches on behavioural skills.

12.36 While we recognize that the range of subjects covered in this training course is basically satisfactory, it does not meet the needs of officers being posted to the principal consular position at most posts abroad. Some officers doing consular work at the missions and some of their supervisors have observed that the course is not adequate. It does not treat some subjects, such as fraud detection in the review of proof of citizenship, in sufficient depth. On the other hand, according to a departmental study, the course is longer than necessary for the numerous employees who take it who will be only marginally involved in consular activities.

12.37 The Department should implement human resources plans that ensure that experienced and trained officers are assigned to consular positions improve the career opportunities of personnel doing consular work, and increase the prominence of consular services within the Department.

12.38 The Department should revise its consular training for personnel assigned abroad to ensure that it meets both the general and specific requirements of the positions to be filled.

Department's response: *We concur. The Department fully recognizes the importance of assigning experienced and trained Consular Officers to consular positions and, to this end, is looking at ways to improve the career prospects of personnel doing consular work.*

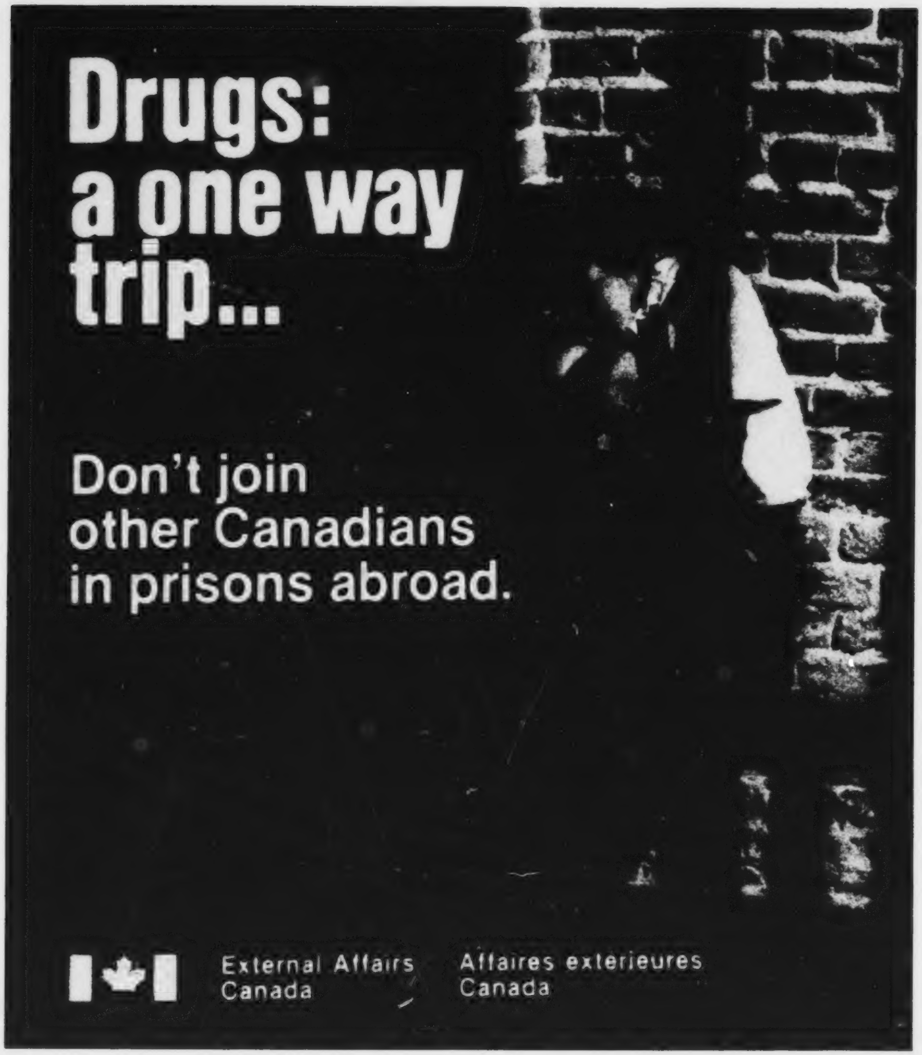
The Department will diversify its training courses for personnel assigned abroad so as to better adapt them to the needs of the positions they are to fill. It will provide a short course to those who will be doing consular work only occasionally and a longer course to those who will be doing mainly consular work.

Public Awareness: Room for Improvement

12.39 The Department conducts public awareness activities to inform Canadians who travel abroad about potential dangers and about the limits to what the federal government can do for them if they get into trouble. It distributes approximately 700,000 copies of a travel information booklet, Bon Voyage... But, with passports issued in Canada and to interested groups on request. The Department also places advertisements in certain travel magazines aimed at travelling Canadians, warning them about smuggling or using drugs while abroad. In addition, many missions produce local tip-sheets on their own initiative which they distribute to tourists.

12.40 In spite of these activities, the Department has not fully exploited the public awareness program's potential to inform Canadians about the dangers of travelling abroad and reduce extra workload at posts. We expected that it would have defined the target groups and ensured that appropriate information is communicated to each group.

Part of the Department of External Affairs' awareness program aims at warning Canadians about the dangers of drug trafficking (see paragraph 12.39).


Drugs: a one way trip...
Don't join other Canadians in prisons abroad.
External Affairs Canada
Affaires exterieures Canada

12.41 Limited distribution of travel information. The Department's current public awareness activities do not reach a large enough segment of the travelling public. The travel information booklet does not reach individual Canadians and tour groups who travel to countries where a passport is not required, such as the United States, Mexico and many Caribbean islands. These countries are the destination of a vast majority of Canadian travellers. The tip-sheets for tourists are only given out to people who visit the missions.

12.42 Need to define and reach target groups. The Department has not identified specific target groups for its public awareness activities and assessed whether the appropriate information is being communicated to each group. In addition, the Department has not assessed the effectiveness of relying on the booklet alone to reach the objectives of its public awareness activities. While we recognize the primary responsibility of travellers to inform themselves of the hazards of travelling and various requirements of other countries, their failure to do so can cause them serious problems and create extra work for the posts abroad. In parts of Asia, we observed instances of workload generated by Canadians who were unaware of local visa and passport regulations.

12.43 Increased public awareness would have at least two important effects. Informed travellers would be less likely to need certain kinds of assistance, thereby saving both the Department and themselves time. Also, the public would have more realistic expectations regarding what services the Department can and cannot provide. The significant workload of posts related to requests for information on where to eat and shop, whether the post will make travel arrangements and where to find a job, would be reduced.

12.44 The Department should define the target groups for its public awareness program and ensure that appropriate information is communicated to each group.

Department's response: *As soon as human and financial resources can be made available, the Department intends to better define the target groups for its public awareness program and ensure that appropriate information is communicated well.*

Honorary Consuls

12.45 Honorary consuls are private individuals who generally provide emergency consular services on a part-time basis to Canadians abroad. They are not expected to deliver the same range and extent of services that missions provide. Canadian posts are responsible for supervising the honorary consuls in their respective jurisdictions. The use of honorary consuls is an inexpensive way to provide certain services in areas of the world where Canada has no regular diplomatic or consular representation. It is less expensive than establishing a regular diplomatic mission or extending services from such a mission to a remote area. In response to budget cutbacks, the Department has increased the number of honorary consuls from 24 in 1984 to 48 in 1989. Many countries make use of the honorary consul system, which is governed internationally by the Vienna Convention on Consular Relations.

12.46 Need to define duties and responsibilities. Honorary consuls work in locations remote from the supervising post, without the benefit of its direct support. Therefore, there is a need for the Department to ensure that expectations concerning the delivery of consular services are spelled out for each of them, that their duties are specifically described, and that their activities are adequately supervised by the posts.

12.47 We observed that, to a large extent, many honorary consuls were left to determine their own responsibilities and the extent of service they will provide. The main risk is inconsistent or unfair treatment of Canadians. As far back as 1983, the Department recognized the need to delineate the responsibilities, duties and prerogatives of its honorary consuls. As their number increases, especially in areas visited by large numbers of Canadians, so do the risks associated with leaving their responsibilities ill-defined.

12.48 Irregular monitoring of honorary consuls. Management monitoring of the activities of honorary consuls does not compensate for the lack of clear specification of duties. Important aspects of a post's supervision of the honorary consuls in its jurisdiction are periodic visits by post staff, monthly reporting, and annual appraisals. We noted that visits were in fact infrequent and that some honorary consuls were not visited for two to three years at a time. Monthly reports contain only information on numbers of cases and hours spent on them. Without defined expectations and duties, the relevance and usefulness of annual appraisals are weakened.

12.49 Risks of exceeding authority. Without clear guidance or adequate field monitoring by the missions, the autonomy of the honorary consuls is such that they may easily exceed their authority. During our visits at posts, we were told that honorary consuls have in certain instances failed to report consular cases to the supervising missions, have refused to take direction from anyone other than the head of post, or have preferred to deal directly with headquarters or with individuals in Canada, bypassing the normal reporting relationship with the mission.

12.50 We also noted instances of honorary consuls exceeding their responsibilities in relation to another mission program. For many years, the Department has been concerned about their involvement in cases of immigration to Canada, yet we noted instances where they were still intervening in these cases.

12.51 Status of "unofficial consular representatives" raises a legal question. Certain missions have hired individuals, called "unofficial consular representatives", to perform the same functions as honorary consuls. In doing so, the Department has entered into contractual relationships of questionable legality. The Act of Parliament that provides the funds for honorary consuls requires that they be appointed by Order-in-Council. The Department has not obtained such approval.

We have identified specific improvements to the management process that would enable the Department to better meet increasing demands for service in an environment of fiscal restraint.

12.52 Giving status to these unofficial representatives to deliver consular services may also violate the international treaty governing consular relations. The Vienna Convention requires that receiving nations must consent to the establishment of consular posts within their borders. The Department has not requested or received the permission of the countries where it has established unofficial consular representatives. The Government of Canada, on the other hand, relies on the other signatory countries to observe the Convention.

12.53 The Department should clearly define the consular responsibilities of honorary consuls and ensure that their delivery of services is monitored.

12.54 The Department should ensure the legality of the hiring and status of "unofficial consular representatives".

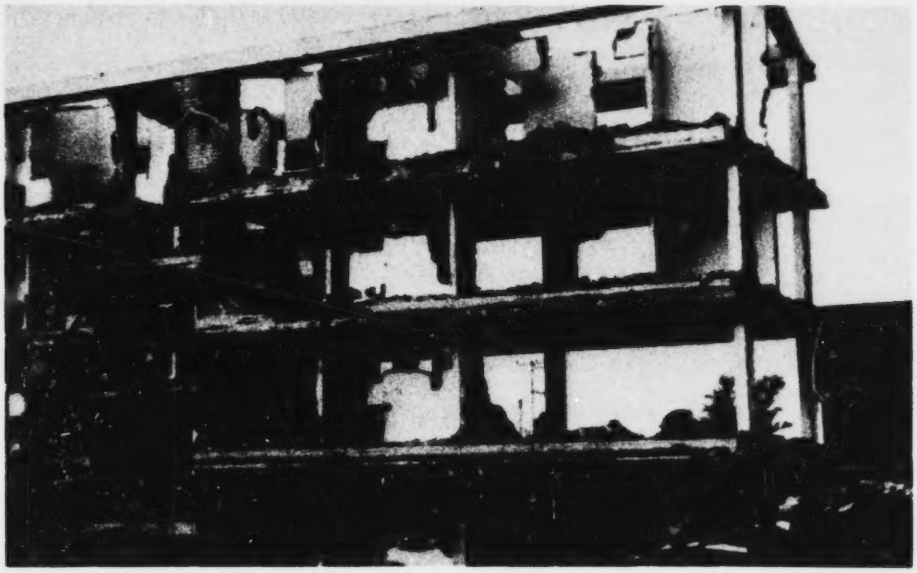
Department's response: *The responsibilities of honorary consuls are defined in chapter XI of the Manual of Consular Instructions. The letter of appointment sent to each new honorary consul on the occasion of his nomination provides the framework for defining more precisely and in more detail the honorary consul's responsibilities. Heads of mission will be instructed to use this letter, as well as other means, to better define the duties of honorary consuls under their jurisdiction.*

Heads of mission will also be reminded of the importance of exercising proper supervision of honorary consuls to ensure an improved delivery of services.

To avoid ambiguity that existed concerning the legality of the status of the unofficial consular representatives, the Department has decided not to renew the contracts of its seven "unofficial consular representatives" abroad. Consular services in these localities will be provided by other means, including, when necessary, the appointment of honorary consuls.

Contingency Planning for Crises Abroad: Many Missions had No Plans

12.55 Canada's missions are required to provide protection and assistance to Canadians during foreign crises such as civil disorders or natural disasters. It is a consular responsibility to develop contingency plans. During an actual crisis abroad, these plans are



The consular staff at Canada's missions abroad provide services to Canadians caught up in foreign crisis situations (see paragraph 12.55).

intended to serve as a basis for informed decision-making by the head of post and headquarters.

12.56 Contrary to departmental requirements that there be a plan for every post, we found that 7 posts out of 33 considered by headquarters as currently facing a medium-to-high risk of a local crisis did not have contingency plans. Over one-third of the remaining missions considered as facing a low risk did not have contingency plans. Recent events in Asia show how quickly a crisis can develop in a country thought to pose little or no risk of civil disorder and, therefore, the importance of developing plans at all posts. For the posts that had developed plans, many were out of date.

12.57 The Department should develop and keep at its posts up- to-date contingency plans that are appropriate to the risk of crisis at each post.

Department's response: *The Department agrees that contingency planning is an important element of the consular program. The seven (7) missions identified are all in the advanced stages of the process of completing their contingency plans. The Department will also ensure that all contingency plans are reviewed and updated on a regular basis.*

Passports Issued by Posts

12.58 Consular officers are responsible for issuing passports, on request, to Canadians who live or travel abroad. In 1988, of the 1,100,000 passports produced, 69,000 were issued abroad. New passports represented 90 percent of those issued abroad, while the remainder were replacements for passports that had been reported lost or stolen.

12.59 Canadian passports can be of great value to foreigners who seek illegal entry into Canada and to others who intend to use them for illegal purposes such as drug smuggling. Some will try to obtain a valid passport through fraudulent documents showing Canadian citizenship; some will try to purchase false passports on the black market. The Department emphasizes that the concern for security must be balanced with cost and the need for expeditious issuance of passports to Canadians. However, it is important that security not be compromised.

12.60 A number of gaps in current control procedures at posts combine to increase the risk of issuing passports to ineligible persons. Current passport procedures require that each applicant submit an application form signed by a guarantor and accompanied by proof of Canadian citizenship, usually a Canadian citizenship certificate or a birth certificate. Validation of the proof of Canadian citizenship and independent assurance of the identity of the applicant are critical in verifying passport applications.

12.61 The Department has put in place at posts abroad various procedures such as a passport control list and a list of valid passports. Moreover, each post has copies of specimens of provincial birth certificates with which it can compare the birth certificate presented by the applicant. In doubtful cases consular officers send a telex to Ottawa requesting additional information.

12.62 During our visits to posts we observed gaps in the passport control procedures. These raise the question of whether security may have been compromised. The gaps were brought to the attention of the Department.

12.63 At the time we completed the audit, the Department had not assessed the risks associated with the gaps. Consular officials told us that these deficiencies are compounded by the fact that, in Canada, passport databases are not tied in with citizenship or immigration databases.

12.64 The Department of External Affairs, in consultation with other appropriate government agencies, should assess whether the current passport control procedures at posts abroad pose an unacceptable risk of passports being issued to ineligible persons.

Department's response: *The Department agrees.*

13

DEPARTMENT OF FINANCE

The Management of Foreign Exchange Operations

13

DEPARTMENT OF FINANCE

The Management Foreign Exchange Operations

Main Points

13.1 Canadian authorities buy and sell foreign currencies to moderate short-term swings in the external value of our dollar. This intervention activity leads to a reduction of foreign exchange reserves when our dollar is depreciating and an increase when it is appreciating (paragraphs 13.19 and 13.20).

13.2 Foreign exchange assets are balanced by public debt, denominated in both foreign currencies and Canadian dollars. Income earned on these assets is generally less than the cost of servicing the associated debt. Thus, managers seek to improve earnings and reduce costs, while ensuring that funds are always available for intervention and that risks are considered (13.26 to 13.28).

13.3 Since 1980, significant amounts of gold held in Canada's foreign exchange reserves have been sold. Proceeds have been retained in reserves and invested in interest-earning foreign currency assets. As well, interest has been earned on gold loans (13.37 to 13.40).

13.4 As foreign reserves grew from early 1987, opportunities were taken to pay down high-cost unmatured debt denominated in foreign currencies. A process for systematic analysis of less obvious investment alternatives is being developed. The feasibility of extending this system to simultaneously evaluate borrowing, liability adjustment, and risk coverage options should be considered (13.33 to 13.35).

13.5 Opportunities to improve returns and reduce costs may entail increased risk. We are suggesting that the feasibility of developing more formal, but flexible, risk guidelines for program managers be examined, along with systems for monitoring risk exposure and evaluating any reaction required (13.44 to 13.53).

13.6 Intervention and foreign exchange operations do not lend themselves to incorporation as part of the government's annual budget and estimates. However, the absence of comprehensible reference material on this subject does nothing to encourage informed and regular parliamentary debate about these operations. We believe that more comprehensive coverage in this area should be developed and clearly presented to Parliament (13.54, 13.55 and 13.81).

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DEPARTMENT OF FINANCE

Management of Foreign Exchange Operations

Background and Audit Scope

Broad Objectives

13.7 International trade and capital flows have always been an important source of economic development, employment growth and improvement in economic well-being in Canada. Orderly exchange markets facilitate such international commerce.

13.8 The broad objective of Canada's exchange rate strategy is to contribute to orderly markets, with emphasis on the external value of the Canadian dollar (C$) relative to its United States counterpart (US$).

Historical Setting

13.9 Toward the end of World War II, major industrialized and trading countries sought to promote stable exchange rates as a means of fostering renewed international commerce. Under the Bretton Woods Agreement, Canada and its major trading partners agreed to abide by a system of fixed, but adjustable, exchange rates. In 1950, Canada alone decided to pursue a floating exchange rate regime. In other respects, we continued to share the goals of the Agreement and to be an active member of the International Monetary Fund (IMF) -- created, in part, to promote the exchange objectives of the accord. Through membership in the IMF, Canada has sought to contribute to these objectives.

13.10 Against a background of severe exchange market pressures, Canada returned to a fixed exchange regime in 1962. Since 1970, however, we have maintained a floating exchange rate.

13.11 In 1973, the Bretton Woods system of fixed exchange rates broke down. Since then an eclectic system has evolved. Under an amendment to the IMF Agreement, member countries are allowed to adopt an exchange rate arrangement of their choice, even though the goal of orderly international monetary conditions remains intact.

13.12 Although the IMF continues to be at the centre of the international exchange and monetary system, in recent years multilateral communication and co-operation between the monetary and exchange authorities of the leading industrial and trading nations has expanded greatly. Canada is an active partner in this.

13.13 Canada's floating exchange rate policy relies on international market forces to determine the basic price of the C$. Since 1970, the strategy of successive Canadian governments has been to intervene in these markets to slow the rise or fall of the C$ compared with the US$. This reflects the assumptions that exchange rate volatility has undesirable economic consequences and that intervention can help reduce such volatility.

The Nature of Intervention

13.14 In the main, intervention consists of buying US$ with C$ to offset upward pressures on the Canadian dollar, or selling US$ for C$ to counter downward pressures on the

Somewhere in the world, at all hours of the day, currency is being exchanged. Uniquely, the Philadelphia currency exchange market is open to do business with all major exchanges, right around the clock (see paragraph 13.13).

external value of the C$. At the moment of intervention, the government has traded one currency asset for another.

13.15 Intervention takes place frequently. Over short periods of time it may involve both the buying and selling of US$ as pressures on the C$ shift. Consequently, the government must have access to substantial amounts of both dollar currencies at all times. U.S. funds are obtained through the issuance of federal government debt denominated in foreign currencies or through the purchase of US$ in the intervention process. The latter leads to increases in C$ debt to fund such purchases.

13.16 The Currency Act provides authority for intervention. It establishes the Exchange Fund Account (EFA) through which intervention takes place and in which most foreign exchange reserves are held. This legislation also specifies general restrictions on the range of assets that may be held by the EFA.

13.17 The Financial Administration Act (FAA) and the annual Borrowing Act(s) provide the legal authority for borrowing and public debt operations, in both C$ and in foreign currency terms.

13.18 Foreign exchange reserves include currencies and other assets in addition to US$, as a result of obligations to support intervention activities on a co-operative international level and other historical and policy factors.

Changing Levels of Foreign Exchange Reserves

13.19 Intervention by Canadian authorities to dampen short-term volatility in the price of the C$ -- called "leaning against the wind" -- also resists somewhat more fundamental pressures toward appreciation or depreciation of the C$. When the C$ is depreciating, sales of foreign exchange outstrip purchases and foreign exchange reserves decline. Eventually, the government may have to borrow foreign currency to replenish reserves.

13.20 Intervention during periods when there is upward pressure on the C$ has the opposite effect. Foreign exchange reserves build up, and debt denominated in foreign currencies tends to be repaid. C$ advances to the EFA and domestic borrowing rise. Exhibit 13.1 illustrates the association between trends in the exchange rate and the rise and fall of public debt payable in foreign currencies.

Recent History

13.21 Since early 1987, with the Canadian dollar strengthening against its U.S. counterpart, purchases of foreign currencies have outweighed sales, and foreign exchange reserves have increased sharply. Some of the increase in reserves has been used, when opportunities have arisen, to pay down public debt denominated in foreign currencies. Exhibit 13.2 provides a picture of the changing level of foreign currency assets in the EFA and of associated foreign-denominated public debt. It also illustrates the net foreign currency position for recent years when the C$ was at first falling and then recovering sharply.

Responsibilities

13.22 The Financial Sector Policy Branch of the Department of Finance is responsible for managing foreign exchange intervention, assets and associated liabilities.

13.23 The Bank of Canada is designated as the government's agent respecting intervention operations and day-to-day management of foreign exchange assets and related liabilities.

Scope

13.24 The audit examined how the Department of Finance manages the portfolio of assets and liabilities associated with Canada's intervention in foreign exchange markets. By and large, this entailed an examination of Exchange Fund Account operations excluding intervention activities per se.

Since 1987, foreign exchange reserves have increased sharply.

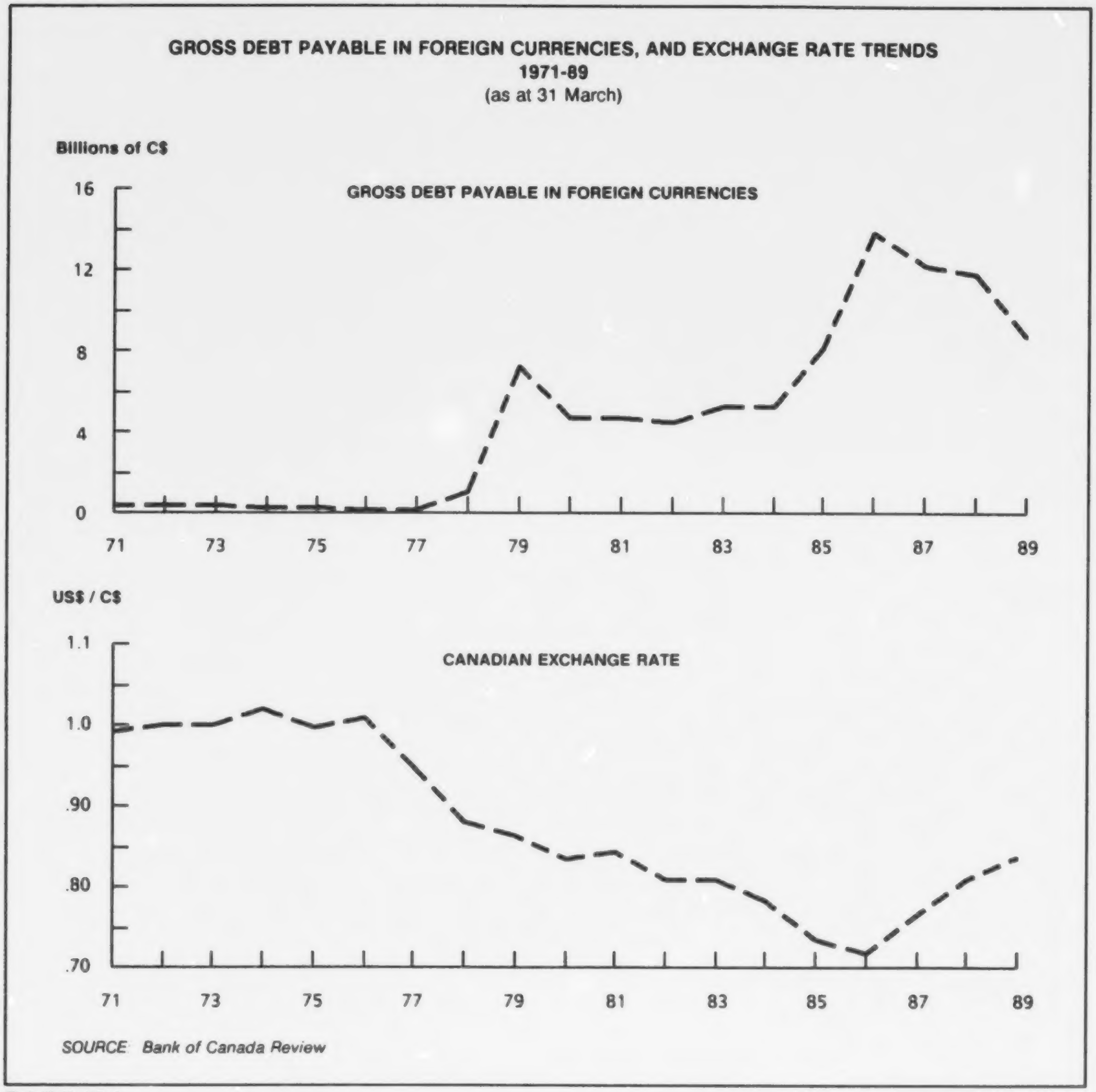
13.25 However, these operations are interrelated with the overall financial operations of the government. Thus we examined the management of Canada's overall financial requirements and its public debt, to the extent that they are affected by advances to the EFA and receipts from intervention activities transacted through the EFA.

13.26 Briefly, increases in foreign reserve advances to the EFA are ultimately financed through government borrowing. On the other hand, C$ purchased in intervention operations are returned and netted against C$ advances. Public debt denominated in foreign currencies is redeemed using foreign currency holdings of the EFA.

Observations and Recommendations

Shifting Managerial Concern

13.27 As shown in Exhibit 13.1, the C$ followed a long, declining path against the US$ until early 1986. During that period, the principal concerns of responsible managers were:

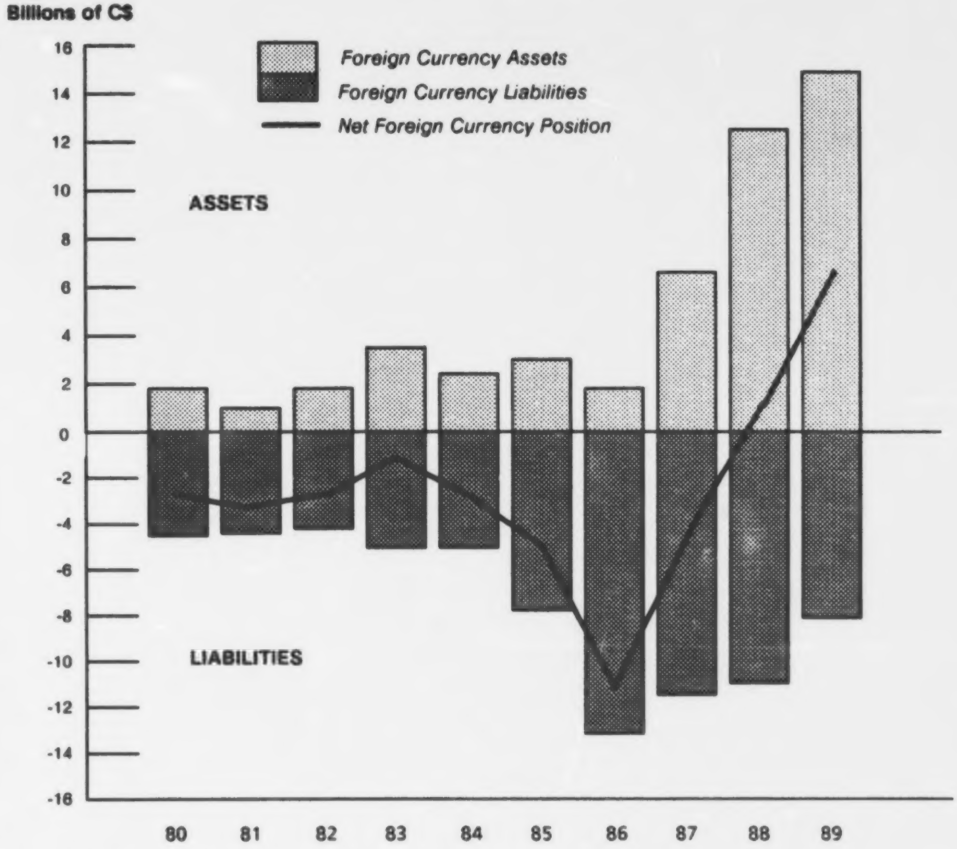


SOURCE: Bank of Canada Review

Exhibit 13.1

- to replenish liquid foreign currency assets in the EFA, through foreign currency borrowing; and
- to ensure quick access to foreign currency, in addition to that held in the EFA, through establishing commercial lines of credit and new, short-term borrowing programs.

13.28 With the growth in international reserves held in the EFA -- from US $2.6 billion at the end of 1986 to US $13.6 billion two years later -- management has also had to consider how to deploy reserves that may not be needed for immediate intervention and how to manage cost-effective adjustments to the stock of existing foreign liabilities.



EXCHANGE FUND FOREIGN CURRENCY ASSETS AND ASSOCIATED LIABILITIES *
1980-89
(as at 31 March)

* Excludes debt assumed from Canadair Financial Corporation Inc.

Source: Public Accounts

Exhibit 13.2

Management Style

13.29 The Financial Sector Policy Branch of the Department of Finance focusses primarily on strategic considerations with much of the day-to-day activity associated with intervention, asset and liability management, and borrowing delegated to the Bank of Canada. The rapid change in the exchange and financial environment in recent years demands more frequent strategic reassessment than in the past.

13.30 The Branch's approach to managing this process is to ensure that it has qualified staff in place to evaluate the changing environment, the advice that it receives from outside sources, and any new or anticipated operational opportunities or constraints. Formal systems and processes for monitoring and review of strategies and operations are not extensively developed nor are they considered necessary by senior Branch officials.

Delineation of Investment Opportunities

13.31 Managers continue to be preoccupied with maintaining ready access to foreign currency for intervention to moderate downward pressure on the C$.

13.32 However, the pressure on the C$ over the last couple of years has, on balance, been upward. This has led to an accumulation of sizeable foreign exchange reserves, both in total and net of liabilities payable in foreign currencies. No evidence was found that this turnabout was anticipated or that processes were in place beforehand to enable managers to evaluate quickly what portions of reserves were available for investment. Although the Currency Act generally specifies assets which may be held in the EFA -- by way of currency and the maximum term to maturity -- formal processes were not in place to consider the full range of alternative placement opportunities.

13.33 Nonetheless, program managers moved to apply expanded reserves to the reduction of high-cost outstanding debt denominated in foreign currencies as opportunities arose.

Expanded foreign reserves allow and challenge managers to improve rates of return and reduce interest costs.

13.34 Moreover, Finance is developing a system to enhance investment income through ongoing evaluation of reserve levels and potential demands on them, particularly the amounts needed to meet intervention requirements under various assumptions about market conditions in the future. This initiative involves officers of the Bank of Canada as well as of Finance.

13.35 Program officers must deal with a growing range of asset placement alternatives, borrowing options and risk coverage techniques. It is unlikely that these can all be regularly considered without support of automated systems. Simultaneous consideration of numerous investment, borrowing and liability adjustment alternatives is now practiced by a number of large private sector portfolio management operations. The government cannot adopt this approach directly because of constraints inherent in the public sector context. However, this added complexity reinforces the argument that systems are needed to assist managers to organize and analyze alternatives in the context of overall program objectives.

13.36 The Department of Finance should consider extending the system currently under development for assessment of investment alternatives to include simultaneous consideration of borrowing, liability adjustment and risk options.

Department's response: *With the recent growth in the level of Canada's international reserves, portfolio management has taken on added significance. As noted in this report a system is currently under development which should assist in the assessment of investment options.*

In considering extending this system or developing a similar system to assist in the management of Canada's foreign-currency-denominated liabilities, it should be noted that apart from Canada Bills, Canada's foreign currency borrowing program is dormant. It has been more than two years since Canada has issued foreign-currency-denominated debt. Foreign-currency borrowings have been few in number, but relatively large in size. The approach taken by the Department has been to carefully analyze the borrowing options available at the time, with currency risk being thoroughly examined prior to issue. At the *present time, from a combined portfolio perspective, risk associated with debt denominated in overseas currencies is minimal.*

Insofar as liability adjustment is concerned, it may be remarked that recent practice has been to repay foreign currency debt as it has fallen due and to take advantage of early repayment options, including purchasing Canada's foreign-currency debt on the open market, when there has been an economic advantage to doing so. Existing unhedged overseas debt is monitored and possibilities for reducing exposure, through swaps, early retirements, or other means are evaluated.

Financial markets evolve, at times significantly and rapidly, and such a system would require frequent adjustment and updating if it were to remain relevant. Taking into account the present level of reserves and access to short-term credit, there would be ample lead time to put such a system in place, should it appear that foreign borrowing could be resumed. Should events unfold along these lines this recommendation would be considered.

The Special Case of Gold Holdings

13.37 Over many years, a variety of government programs -- including support for Canada's gold mining industry -- led to an accumulation of gold inventories which peaked at over 33 million fine ounces at the end of 1965. Canada's gold reserves are held in the EFA, although they serve no active role in foreign exchange market intervention.

13.38 Gold has earned only modest amounts of interest -- through the gold loans program; however, the amount has increased steadily. Although it would not be possible to quickly convert all of the approximately 17 million fine ounces of gold currently held in the EFA to interest-earning securities, the interest that could have been earned on the roughly C$ 7.8 billion -- at market prices -- held as gold reserves at 31 March 1989 would have been about C$ 800 million this year alone. Moreover, conversion to foreign currency -- approximately US$ 6.5 billion -- would increase by about 50 percent the Exchange Fund's holding of liquid foreign currency assets available for intervention purposes.

13.39 From the outset of the 1980s, the government has actively managed its gold reserves. This has involved periodic sales of bullion to the market; 5.0 million fine ounces yielding US$ 2.4 billion (C$ 2.9 billion) excluding accumulated interest earnings, were sold during the period 1980 through 1988. The timing and scale of bullion sales have been keyed to market conditions, while avoiding a discernible pattern which could fuel speculation.

13.40 As well, a gold loan program has been developed, with income of C$ 7.1 million in 1988. Since gold holdings could not be sold off quickly without a severe adverse effect on gold prices, low-risk use of the remaining balances can yield substantial incremental revenues, even at low interest rates. Gold loans to financial institutions have expanded rapidly in the last several years.

13.41 We found that the objectives of the gold sales and the gold loans programs are being pursued with diligence. Incremental earnings from the gold loan program and from interest earned on the invested proceeds of gold sales are large. Interest earned on the proceeds of gold sales since the inception of the program in 1980 is estimated by Finance at US$ 1.4 billion.

13.42 The gains on gold sales, which represent the difference between market and book value at the time of sale, are included as part of the net valuation gains (losses) of the EFA. However, Exhibit 13.3 below presents such gains separate from annual gains and losses recorded for other EFA assets. At the end of 1988, the book value was C$ 56 per fine ounce while the market value was C$ 489 per ounce. Clearly, realized gains on sales of large quantities of gold can overshadow valuation gains and losses associated with the management of assets and liabilities involved in intervention operations. They tend to obscure the need for effective management practices in this area.

Risk Management

13.43 **Valuation gains and losses.** The valuation data presented in Exhibit 13.3 reflect the changing C$ value of EFA assets and associated liabilities, including gains and losses from intervention activity.

13.44 The value of foreign exchange reserves and associated liabilities will rise and fall with changes in exchange rates. For instance, the US$ assets acquired before the fact will be worth less in terms of C$ following an increase in the price of the C$, and vice versa. The valuation impact on liabilities will be opposite to the effect on assets. Thus, if assets and liabilities are equal for any one currency, there will be no valuation gains and losses, even as the C$ moves in relation to it. The net liability position for any one currency (or set of highly correlated currencies) is thus the major factor in determining the government's exposure to currency losses or gains.

13.45 While valuation gains on net holdings of assets and liabilities denominated in overseas currencies were recorded in earlier years, valuation losses have been incurred in recent years, as shown in Exhibit 13.3. This reflects the general decline in the value of the C$ compared to the overseas currencies in which Canada has issued public debt for EFA purposes and the excess of liabilities over assets held in these currencies during this period.

13.46 **Risk-reward trade-offs.** There has been no need to issue long-term foreign currency liabilities for over two years. However, previously the government approved borrowing in overseas currencies to take advantage of lower interest rates. This exposed the government to the risk of loss if the US$ declined and to the opportunity for capital gains if it rose against the foreign currency in question. Finance estimates indicate that interest cost savings have exceeded net valuation losses on overseas currency debt issues that were not immediately converted to US$ liabilities; however, these savings do not show up in the accounts, while the valuation losses do.

13.47 Managers in the Financial Sector Policy Branch at Finance have sought to reduce exposure to exchange losses, while minimizing interest costs through borrowing in overseas currencies. For more recent issues, both the liability and currency are converted into US$ at the time of issue.

13.48 However, similar efforts to protect against currency risks on uncovered, outstanding foreign liabilities have not been made. This is partly because the values of assets and liabilities denominated in overseas currencies fortuitously have converged, leading to greater coverage of currency risk. Liabilities denominated in overseas currencies have been deliberately reduced. However, the increase in assets denominated in the same currencies is largely coincidental. EFA holdings of assets denominated in overseas currencies reflect policy decisions concerning Canada's involvement in co-operative international undertakings rather than investment considerations or moves to reduce currency risks.

13.49 The most complex and important challenge for managing assets and liabilities denominated in several currencies is the determination of an "acceptable" degree of risk-taking arising from exchange rate fluctuations. However, there are other risks and opportunities that may affect revenues and costs. For example, decisions based on correct anticipation of future interest rate trends can improve investment returns and reduce

EXCHANGE FUND ACCOUNT NET VALUATION GAINS (LOSSES)*
1984-88
(year ended 31 December)

	1984	1985	1986	1987	1988
			(millions of C$)		
FOREIGN CURRENCIES					
Japanese Yen	$ 23	($ 324)	($ 441)	($ 520)	$ 255
Swiss Francs	92	(290)	(295)	(177)	216
Deutsche Marks	4	(31)	(29)	(17)	32
Overseas subtotal	*119*	*(645)*	*(765)*	*(714)*	*503*
US Dollars	(68)	169	168	263	(249)
Currencies subtotal	*51*	*(476)*	*(597)*	*(451)*	*254*
GOLD	(5)	(142)	107	102	(152)
SPECIAL DRAWING RIGHTS	1	(30)	(7)	8	(71)
NET VALUATION GAINS (LOSSES) EXCLUDING GOLD SALES	47	(648)	(497)	(341)	31
GAIN ON GOLD SALES	14	12	196	641	647
NET VALUATION GAINS (LOSSES)	$ 61	($ 636)	($ 301)	$ 300	$ 678

* Includes valuation gains (losses) on international reserves held in the EFA and associated unmatured public debt denominated in foreign currencies.

Source: Public Accounts

Exhibit 13.3

interest costs on debt. On the other hand, there is an obvious risk that interest rates will move in the opposite direction. Another consideration is that losses, or gains, may result if investments must be converted to cash before maturity in order to fund intervention transactions.

13.50 Two fundamental and interrelated strategic questions should be addressed:

- To what extent should the government take risks and seek gains when managing assets and liabilities denominated in foreign currencies?
- To what extent should managers be directed to seek to minimize interest costs of borrowing in foreign currencies and to maximize returns on the investment of EFA assets, given the primacy of meeting liquidity needs for intervention?

13.51 Senior management of the Department should examine the feasibility of developing formal guidelines for program managers to give them parameters of risks and rewards within which to operate. These guidelines should cover borrowing, managing debt, and investing EFA resources not immediately required for intervention purposes, in assets denominated in foreign currencies. They should be reviewed regularly and adjusted when warranted.

Department's response: *As noted in the response to the previous recommendation (paragraph 13.36), Canada's foreign-currency borrowing program is essentially dormant and overseas currency risk is at a low level. The Department would be willing to consider* *the development of more formal guidelines in this area if it appears likely that the foreign-currency borrowing program would be reactivated.*

While the Department is willing to examine the feasibility of developing more formal guidelines in the other areas mentioned in this recommendation, it should be noted that currency risk is inherent in the operation of an exchange fund. The currency composition of Canada's international reserves is largely a consequence of intervention activity - which is the raison d'être of the Exchange Fund. Opportunities to alter the currency composition of Canada's reserve assets on portfolio grounds are limited, if the underlying purpose of the Exchange Fund and Canada's international obligations are to be respected.

13.52 Officers at Finance evaluate periodically the extent to which liabilities in overseas currencies are covered by assets denominated in the same, or highly correlated, currencies. Options for reducing the liability portfolio to counter imbalances -- currency risk exposures -- are presented for consideration. Assets denominated in overseas currencies are determined largely by policies on multilateral co-operation. Moreover, the number of options for manipulating the portfolio of unmatured debt denominated in foreign currencies is increasing. Under these conditions, there is a need for ongoing monitoring of risk exposure and evaluation of options for risk control. Moreover, such a process might logically extend to other risk-reward considerations.

13.53 Formal systems should be in place at the Department of Finance for monitoring and evaluating risk or opportunity positions from the perspective of assets, liabilities and the combined portfolio. A process that updates operational constraints should be included; for example, the redefinition of holdings of overseas currencies required for co-operative international intervention should be a priority.

***Department's response**: The EFA's net foreign currency position is monitored and evaluated periodically, with full account taken of the operational constraints in place. The Department will examine the feasibility and cost-effectiveness of putting a system in place to make this process more formal and regular.*

As noted in the response to the second recommendation (paragraph 13.51), portfolio considerations can only play a limited role in influencing the currency composition of the Exchange Fund's assets. The nature of the Exchange Fund's operations is such that operational constraints do not change frequently; nevertheless, the Department will consider establishing a more formal process of updating or reaffirming existing constraints. For foreign currency liabilities, see the responses to the first and second recommendations (paragraphs 13.36 and 13.51 respectively).

Information to Parliament

13.54 Although parts of the story about foreign exchange market intervention and management of Canada's foreign exchange assets and liabilities may be found in public documents, there is no comprehensible, consolidated discussion of the operations underlying this important macroeconomic policy area. Indeed, published financial data, even including explanatory notes, cannot reveal the quality of managerial performance, particularly cost-saving achievements.

13.55 Accountability depends on both Parliament and senior government managers having a clear idea of the objectives to be achieved and the performance of those responsible for meeting them. This is particularly important since EFA operations cannot be projected with confidence and, therefore, they are not examined by Parliament as part of the annual budget and estimates process. This section provides a general outline of some of the information that might be included, in more complete form, in improved reporting to Parliament.

13.56 **Canadian dollar defence fund.** The foreign exchange reserves of Canada are now very high compared with recent years. Exhibit 13.4 illustrates the level and growth of these reserves in terms of US$ which form the bulk of all foreign currency assets in the EFA.

13.57 The foreign currency assets held in the EFA are the principal resources used in the intervention process. They are also the EFA's primary base on which investment income is earned. Special Drawing Rights of the IMF are used to settle accounts with the IMF but seldom for intervention-related purposes.

13.58 As discussed previously, gold is not used in intervention. However, since a high level of reserves has a strong psychological value in discouraging speculation against the C$, inclusion of gold in reserves supports the program's objective and is consistent with international practice. Exhibit 13.4 adds to the book value of EFA gold stocks the additional value that would be expressed if they were valued at full market prices.

13.59 If the C$ came under prolonged downward pressure and our foreign currency assets became depleted, Canada could obtain additional foreign currency, under set conditions, through several standby arrangements now in place.

13.60 Canada has commercial line-of-credit arrangements with two consortia of financial institutions -- one Canadian, the other international. The total arrangement is now for US$ 7 billion, down from US$ 7.5 billion several years ago. These facilities have not been activated for over two years, and the Department does not anticipate that they will be called on in the near term. The standby charges on these lines of credit -- US$ 6.7 million in 1988 -- have been negotiated downward in recent years.

13.61 Program managers perceive the remaining arrangements for access to foreign currencies, as shown in Exhibit 13.4, as sources of "last resort". The Bank of Canada - New York Federal Reserve arrangement was twice called on when Canada was on a fixed exchange rate during the 1960s. A review of undertakings during periods of severe exchange difficulties in the past leads us to assume that it may be possible to expand this arrangement and to establish similar accords with other central banks and national treasuries should conditions attached to them be politically acceptable.

13.62 The IMF borrowing rights derive from Canada's membership in that organization. Initial borrowing rights are unconditional and available on demand. Subsequent provisional rights, on the other hand, would be extended only if Canada were to agree to terms and conditions concerning the management of the domestic economy.

13.63 Canada's capacity to defend the external value of its currency is at an historically high level. Reserves and back-up access to foreign funds may well exceed intervention needs for some time into the future. This situation requires that managers actively seek to ensure that assets are earning appropriate returns and that debt servicing costs are reduced where possible. Thus comprehensible and complete reporting on reserve positions and prearranged access to foreign currencies is important.

13.64 **Borrowing capacity.** Like line-of-credit arrangements, well developed borrowing programs can be thought of as substitutes for holding foreign currency reserves.

13.65 Long-term borrowing alternatives are not being considered by officials at Finance in any systematic way. They do not consider that there is a need to do so, given current high foreign exchange reserve levels.

ASSETS OF THE EXCHANGE FUND ACCOUNT AND BACK-UP ARRANGEMENTS FOR ACCESS TO FOREIGN EXCHANGE

1985-89

(as at 31 March)

	1985	1986	1987	1988	1989
			(millions of US$)		
EXCHANGE FUND ACCOUNT (EFA) ASSETS					
Foreign Currencies/Assets	$ 2,189	$ 1,305	$ 5,026	$ 10,145	$ 12,492
International Monetary Fund (IMF)*	199	373	390	928	1,346
Gold (book value)	699	601	874	893	770
Subtotal (book value)	*3.087*	*2.479*	*6.290*	*11.966*	*14.608*
Additional Value of EFA Gold at Market Price	5,932	6,115	7,303	7,513	5,752
Subtotal (market value)	*9.019*	*8.594*	*13.593*	*19.479*	*20.360*
BACK-UP ACCESS					
Commercial Banks: Total Lines of Credit	7,500	7,500	7,500	7,000	7,000
Bank of Canada-New York Federal Reserve Bank: Reciprocal Arrangement	2,000	2,000	2,000	2,000	2,000
IMF-Automatic Rights	662	731	688	591	458
IMF-Provisional Rights	2,876	3,391	3,772	4,080	3,847
Subtotal	*13.038*	*13,622*	*13,960*	*13,671*	*13.305*
TOTAL EFA ASSETS AND BACK UP (market value)	**$ 22.057**	**$ 22.216**	**$ 27.553**	**$ 33.150**	**$ 33.665**

* Includes Special Drawing Rights and IMF Notes

Source: Public Accounts, Bank of Canada Review, New York Federal Reserve Bank Quarterly Reports

Exhibit 13.4

13.66 On the other hand, Canada has developed an ongoing short-term borrowing program over the last several years. The Canada Bills program has an outstanding debt balance of approximately US$ 1 billion, which is continuously rolled over to keep the program active. The objective is to have an economic, efficient and expandable short-term borrowing program as insurance that foreign currency can be raised if and when required. On balance, there is little if any net cost to the public purse; interest rates on Canada Bills borrowing are virtually identical to those earned on short-term investments denominated in US$. This program has been launched, maintained and evaluated in a very thorough fashion. However, its effectiveness in times of real need cannot be fully predicted from its performance during the past several years when there was relatively little downward pressure on the C$.

13.67 Performance measurement. We found that goals and objectives are specified for certain individual programs and activities within foreign exchange operations, and the achievements of their intended results are assessed.

13.68 For the foreign currency asset and liability portfolio as a whole, the overriding mission to be fulfilled is to maintain a capacity to intervene quickly to counter any downward pressure on the Canadian dollar. Understandably, given a decade of low reserve levels from the mid-1970s through 1986, there is much less clarity about operational constraints and secondary objectives such as cost minimization, revenue maximization and risk-reward tradeoffs.

13.69 As well, over the past five years there has been a rapid expansion of investment, credit and risk coverage alternatives available to portfolio managers. In this setting, Finance and the Bank of Canada have both recognized the need to develop more formal and automated accounting, portfolio information and analysis, and performance measurement systems. A substantial effort has recently been launched to meet this need, in part by modifying software systems developed for private sector operations. Such systems should be of assistance in the ongoing management of the Exchange Fund and related operations and in reporting to Parliament.

13.70 **Program costs.** Parliamentarians have recently inquired into the cost to taxpayers of maintaining foreign exchange reserves.

13.71 Recent analysis in this area indicates that Canadian intervention and foreign exchange reserve operations may generate net revenues over the long term, although this conclusion depends on the time period considered. However, there is no accounting presentation that provides that information. It would seem reasonable that the Department should report all income and costs associated with these operations to Parliament, as fully as possible.

Full income and cost information on foreign exchange operations should be reported to Parliament.

13.72 Exhibit 13.5 provides detail on the annual income of the EFA for the past five years. Investment income has grown sharply with the dramatic run-up in reserves over the past two years. Net valuation adjustments moved from a loss position in 1985 and 1986 to a gain position in 1987 and 1988, partly because of the appreciation of the C$ but largely as a result of exceptionally large gains on gold sales in the latter two years (see Exhibit 13.3).

13.73 Exhibit 13.6 is intended only as an approximation of the scale of costs involved in intervention and in the maintenance of foreign exchange reserves, not as a definitive measure of this operation.

13.74 In Exhibit 13.6 gains from gold sales (Exhibit 13.3) are deducted from the gross income (Exhibit 13.5) to show the net operating loss or income position of the EFA.

13.75 Interest payable in foreign currencies has come down since 1986 as debt denominated in foreign currencies has matured and otherwise been redeemed, as shown in Exhibit 13.6.

13.76 To this point, only the costs of servicing debt denominated in foreign currencies are included in Exhibit 13.6. However, intervention transactions also involve C$ receipts and disbursements and, respectively, the associated interest earnings and expenses are part of the total costs of intervention and maintenance of foreign exchange reserves.

13.77 When the C$ is depreciating and intervention leads to net purchases of C$ with foreign currencies, foreign exchange intervention will be making a net contribution of C$ to meet the government's financial requirements. When the C$ is appreciating and intervention leads to net sales of C$ against foreign currencies, there will be a net draw on the Consolidated Revenue Fund (CRF). In Exhibit 13.6, we show the interest on the EFA's Canadian dollar deposit position with the Receiver General for Canada -- which provides a running total of C$ drawings on and refunds to the CRF. It is shown as a reduction in interest costs when the balance is positive and an additional interest cost when the balance is negative.

13.78 The data and estimates presented in Exhibits 13.5 and 13.6 could be interpreted further. For example, higher levels of foreign exchange reserves do not alter the fact that

EXCHANGE FUND ACCOUNT INCOME
1984-88
(year ended 31 December)

	1984	1985	1986	1987	1988
			(millions of C$)		
INVESTMENT INCOME					
Cash & Short term Deposits	$ 69	$ 42	$ 46	$ 128	$ 234
US Dollar Securities	150	118	104	249	691
Subtotal	*219*	*160*	*150*	*377*	*925*
Special Drawing Rights	6	9	15	30	65
International Monetary Fund Notes	27	23	19	19	11
Subtotal	*33*	*32*	*34*	*49*	*76*
Gold Loans	-	2	3	3	7
Total Investment Income	252	194	187	429	1,008
NET VALUATION GAINS (LOSSES)	61	(636)	(301)	300	678
NET EXCHANGE FUND ACCOUNT INCOME (LOSS)	**$ 313**	**($ 442)**	**($ 114)**	**$ 729**	**$1,686**

Source: Public Accounts

Exhibit 13.5

total interest costs (Exhibit 13.6) continue to exceed the total investment income (Exhibit 13.5). We believe that further analysis of such fundamental information would be of interest to Parliamentarians and could be developed by the Department of Finance.

13.79 The cost of maintaining all foreign exchange assets, those in the EFA as well as in other accounts, would also include:

- the net costs of Canada's financial position with the IMF,
- the standby charges for commercial lines of credit, and
- the relevant operating costs of the Department of Finance and the Bank of Canada.

13.80 It is the nature of financial statements to duly record costs entailed in operations. However, no estimates are presented to the public that indicate the extent of savings that have been realized over the years from efforts to reduce interest and other carrying costs. In providing comprehensive reports to Parliament this feature of performance might well be included.

13.81 The annual report on the Exchange Fund Account and other official publications should be enhanced to provide Parliament with a complete and comprehensible picture of:

SUMMARY OF MAJOR COSTS AND INCOME ASSOCIATED WITH FOREIGN EXCHANGE OPERATIONS
1985-88
(year ended 31 December)

	1985	1986	1987	1988
	(millions of C$)			
EFA OPERATIONS				
Annual EFA Net Loss (Income) (1)	$ 454	$ 310	$ (88)	$(1,039)
INTEREST COSTS				
Interest on Outstanding Debt Payable in Foreign Currencies (2)	835	1,021	976	840
Imputed Interest Costs (Income) on EFA Canadian Dollar Deposits with the Receiver General (3)	(450)	(779)	(384)	377
Total Interest Costs	385	242	592	1,217
ESTIMATED NET COSTS ASSOCIATED WITH FOREIGN EXCHANGE OPERATIONS	**$ 839**	**$ 552**	**$ 504**	**$ 178**

(1) Excluding gains on gold sales

(2) Estimates based on debt charges for fiscal year ended 31 March, excluding debt assumed from Canadair Financial Corporation Inc.

(3) Costs are included in Public Accounts as part of public debt charges although the number presented here is an estimate. The imputed income statistics are not reflected in Public Accounts. They are notional values in that they represent the amounts by which public debt charges would have been higher, had C$ received from sale on foreign exchange not been used to fund the government's financial requirements.

Source: Public Accounts, Bank of Canada Review. Department of Finance records

Exhibit 13.6

- **the full extent of foreign exchange reserves and offsetting liabilities or debts, and back-up access to foreign currency;**
- **the net costs of maintaining these reserves and back-up arrangements, including trading profits (losses) arising from intervention; and**
- **the performance of the program.**

Department's response: *The Department will give further consideration to this suggestion. It notes, however, that considerable information relating to Canada's international reserves, foreign currency liabilities, and the operations of the Exchange Fund is available to Parliament and the general public. It is also the Department's understanding that, by international standards, Canada is relatively open about these matters. Requests for additional information, of the type suggested in the recommendation, have been infrequent.*

14

DEPARTMENT OF FINANCE

Tax Collection Agreements

14

DEPARTMENT OF FINANCE

Tax Collection Agreements

Main Points

14.1 Under the tax collection agreements, the federal government collects individual income taxes on behalf of all provinces and territories except Quebec and corporate income taxes for all provinces and territories except Quebec, Ontario and Alberta. Taxes collected on behalf of the provinces and territories for 1987-88 were about $20 billion (paragraphs 14.7, 14.10, 14.25).

14.2 The government's accountability to Parliament for the policy framework for, and administration of, the tax collection agreements should be improved; little useful information is currently provided to Parliament. Reporting to the provinces is generally in accordance with the agreements (14.24 to 14.32, 14.40).

14.3 The agreements have not been kept up to date. Also, the flat rate taxes administered by the federal government on behalf of three provinces contravene a specific provision of the agreements (14.33 to 14.39).

14.4 The methodology used by the Department of Finance in estimating provincial income taxes could be strengthened to reduce the possibility of significant underestimation or overestimation of interim payments to the provinces (14.41 to 14.47).

14.5 There are weaknesses in the existing accounting practices and procedures for estimating the tax collections attributable to the provinces, as reflected in the Provincial Tax Collection Agreements Account. This Account forms part of the financial statements of Canada. No one group within the federal government takes full responsibility for the Account as a whole (14.48 to 14.55).

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Accountability to Parliament is weak (14.24)
The tax collection agreements are not up to date, and some tax measures are being administered without proper authority (14.33)
Reporting to the provinces is in accordance with the agreements and payments are made on a timely basis (14.40)
Procedures for estimating payments to the provinces could be strengthened (14.41)
There are weaknesses in the existing accounting practices and procedures related to the Provincial Tax Collection Agreements Account. This account forms part of the financial statements of Canada (14.48)

Exhibits

14.1 Provincial Income Tax Revenue as a Percentage of Total Income Tax Revenue in Canada
14.2 Extract from Public Accounts of Canada, 1987-88
14.3 Net Underestimation/(Overestimation) of Interim Payments of Income Taxes to the Provinces
14.4 Underestimation/(Overestimation) of Tax Collections Attributable to the Provinces at Year End

DEPARTMENT OF FINANCE

Tax Collection Agreements

Introduction

14.6 Tax collection agreements between the Government of Canada and the provinces are an integral part of the general framework of federal-provincial fiscal relations. This framework includes Equalization Payments, Established Programs Financing, and other intergovernmental transfers.

14.7 Under the agreements, most of which were implemented in 1962, the federal government collects individual and corporate income taxes on behalf of the participating provinces and territories and remits to them taxes assessed under their respective income tax acts.

14.8 The remittances do not equal collections because they are based on taxes assessed under the provincial tax legislation and some of the taxes assessed are not recovered from taxpayers. The federal government assumes the cost of bad debts as well as the cost of administering the tax collection agreements. On the other hand, it retains interest and most penalties levied on taxpayers.

14.9 The federal government collects provincial income taxes subject to two main conditions. First, the provinces must use, as a basis for calculating their taxes, the basic federal tax for individuals and taxable income for corporations, as defined in the federal Income Tax Act. Second, the provinces must apply their tax as a constant percentage of basic federal tax or corporate taxable income.

14.10 Authority for the tax collection agreements is in Part III of the Federal-Provincial Fiscal Arrangements and Federal Post-Secondary Education and Health Contributions Act Participation by the provinces and the federal government is entirely voluntary. At present, all provinces and territories except Quebec have agreements with the federal government for collection of individual income tax. Quebec, Ontario and Alberta collect their own corporate tax, and the federal government collects for the rest of the provinces and territories. The agreements vary only slightly from province to province.

14.11 According to the data obtained from the Departments of Finance and National Revenue - Taxation, the provinces participating in the tax collection agreements for corporate tax, which exclude Alberta, Ontario and Quebec, account for less than 20 percent of the corporate taxable income in Canada. On the other hand, with only Quebec administering its individual income tax, over 75 percent of individual taxable income is earned by residents in provinces that are participants.

Evolution of Tax Collection Agreements

14.12 Since 1962, the provinces' share of total income tax revenue has increased substantially due largely to the federal government giving additional "tax room" to the provinces. Exhibit 14.1 shows that their share rose from 18 percent in 1962 to 38.6 percent in 1987. The provinces' increasing reliance on income tax revenue has resulted in pressure for greater flexibility in the system of tax collection agreements.

Increasing importance of income tax revenue to the provinces

PROVINCIAL INCOME TAX REVENUE AS A PERCENTAGE OF TOTAL INCOME TAX REVENUE IN CANADA (SELECTED YEARS)

Year	Percentage
1962	18.0
1967	27.9
1972	29.3
1977	36.9
1982	37.1
1987	38.6

Source: *Calculations from Statistics Canada, National Income and Expenditure Accounts (various issues).*

Exhibit 14.1

14.13 In response to the provinces' desire for greater flexibility to pursue provincial policy objectives and to generate increased tax revenue, the federal government has accepted modifications to the original framework of the agreements. There are now a large number of provincial tax measures administered by the federal government, including tax credits, rebates, surcharges and -- more recently -- flat rate taxes.

14.14 The flat rate taxes, which are applied on the net income of individuals for Saskatchewan and Manitoba and on taxable income for Alberta, represent a major move away from a basic principle of the tax collection agreements, namely determining provincial income tax as a percentage of the basic federal tax. The federal government regards the flat rate taxes as temporary experimental measures.

14.15 The objectives of the tax collection agreements, which have been formally agreed to by the federal government and individual provinces, are contained in the agreements. These are stated in terms of economical and expeditious administration of the provincial income tax acts and facilitation of the payment of taxes imposed under them.

14.16 Other objectives have, however, been mentioned elsewhere by the federal government. Federal-Provincial Programs and Activities -- A Descriptive Inventory 1987-88, a publication of the Federal-Provincial Relations Office of the Government of Canada, describes the federal objectives as:

to prevent unnecessary duplication in the application of income tax systems by the federal and provincial orders of government, to reduce taxpayer confusion and to contribute to the maintenance of a relatively uniform income taxation system across Canada.

14.17 The Minister of Finance in his submission to the 1981 Parliamentary Task Force on the Federal-Provincial Fiscal Arrangements in the Eighties, outlined three guidelines for the admissibility of provincial tax measures, in order to preserve the objectives of the agreements. These guidelines deal with the impact of tax measures on effective administration, harmony and uniformity of the income tax systems, and avoidance of barriers to normal interprovincial investment flows.

Administration

14.18 The Departments of Finance and National Revenue - Taxation together administer the tax collection agreements. The Department of Finance has the overall responsibility for tax collection policy.

14.19 In the Department of Finance, two divisions are involved. The Federal-Provincial Relations Division provides advice to the Minister of Finance on federal policy concerning the tax collection agreements, negotiates and renegotiates agreements with individual provinces, and administers payments of income tax revenue to the provinces. The Fiscal Policy Division produces forecasts of basic federal tax for the individual income tax, and taxable income for the corporation income tax, which provide the basis for calculating payments to the provinces by the Federal-Provincial Relations Division.

14.20 National Revenue - Taxation administers the provincial income tax legislation on behalf of participating provinces, including collecting and assessing provincial taxes. This process is closely integrated with the administration of the federal Income Tax Act, which enables taxpayers to file one tax return covering both federal and provincial income taxes.

14.21 The Department of Supply and Services does a part of the accounting for the Provincial Tax Collection Agreements Account. It credits the account with the provincial portion of estimated income taxes collected.

Audit Scope

We examined how the Department of Finance administers the tax collection agreements.

14.22 Our audit focussed principally on the Department of Finance's administration of the tax collection agreements. Our review of National Revenue-Taxation at this time was limited to interviews with officials.

14.23 We reviewed briefly the activities of the Department of Supply and Services in accounting for the estimated collections owing to the provinces. We also interviewed officials of four provinces for a provincial perspective on the administration of the agreements.

Observations

Accountability to Parliament is weak

14.24 The Federal-Provincial Fiscal Arrangements and Federal Post-Secondary Education and Health Contributions Act contains no specific provision for the accountability of the federal government to Parliament in respect of the tax collection agreements. The government itself has done little to advise Parliament about how well the agreements are working.

14.25 The tax collection agreements program is a significant undertaking of the Government of Canada. The government collected about $89 billion in income taxes for 1987-88, of which about $20 billion pertained to the provincial taxes. This undertaking involves a considerable federal effort, entailing costs and generating benefits for which the federal government should be accountable to Parliament.

Accountability to Parliament is weak.

14.26 Accountability to Parliament requires a reporting of the objectives of the federal government in respect of the tax collection agreements, the resources required to administer them and the results achieved.

14.27 The only regular reporting to Parliament on tax collections, however, is in Sections 2 and 8 of Volume 1 of the Public Accounts 1987-88. In the Statement of Assets and Liabilities of Canada in Section 2, the current and previous years' balances in the Provincial Tax Collection Agreements Account are given. Section 8 contains a brief summary of the nature of the agreements. It also contains a table, shown in Exhibit 14.2, providing data that are difficult to understand without explanation.

14.28 Furthermore, there is no reporting to Parliament giving the basis on which payments to the provinces were calculated, the magnitude of any revisions in payments with respect to prior years, or the reasons for any revisions to payments.

14.29 There is no mechanism for reporting to Parliament on all provincial tax measures administered by the federal government from time to time. No information on the tax collection agreements is included in Part III of the Department of Finance's Main Estimates. The only information provided in National Revenue - Taxation's Part III is a list of provincial tax incentives administered by that department. There is no information on such measures as surtaxes, flat rate taxes and tax reductions administered on behalf of the provinces.

14.30 Neither the Department of Finance nor National Revenue-Taxation could provide us with the estimated cost of administering the tax collection agreements. The Department of Finance advises that in furtherance of the economy objective of the agreements, the administration of the federal and provincial income tax acts is integrated. Because of this integration, the Department stated that it is difficult to determine separately actual costs of administration of the tax collection agreements. We believe, however, that certain costs, such as bad debts, could be estimated. In 1988-89, the federal government wrote off $211 million as income tax bad debts and there was an allowance for accounts of doubtful collectibility at the end of that year of over $1.6 billion. (These figures exclude amounts relating to Scientific Research Tax Credits.) A portion of the write-off and the allowance would pertain to the provincial income taxes. However, no information on these elements is provided to Parliament.

14.31 While there has been no evaluation of the tax collection agreements system since its inception in 1962, the Department of Finance has occasionally carried out reviews of specific elements of the agreements.

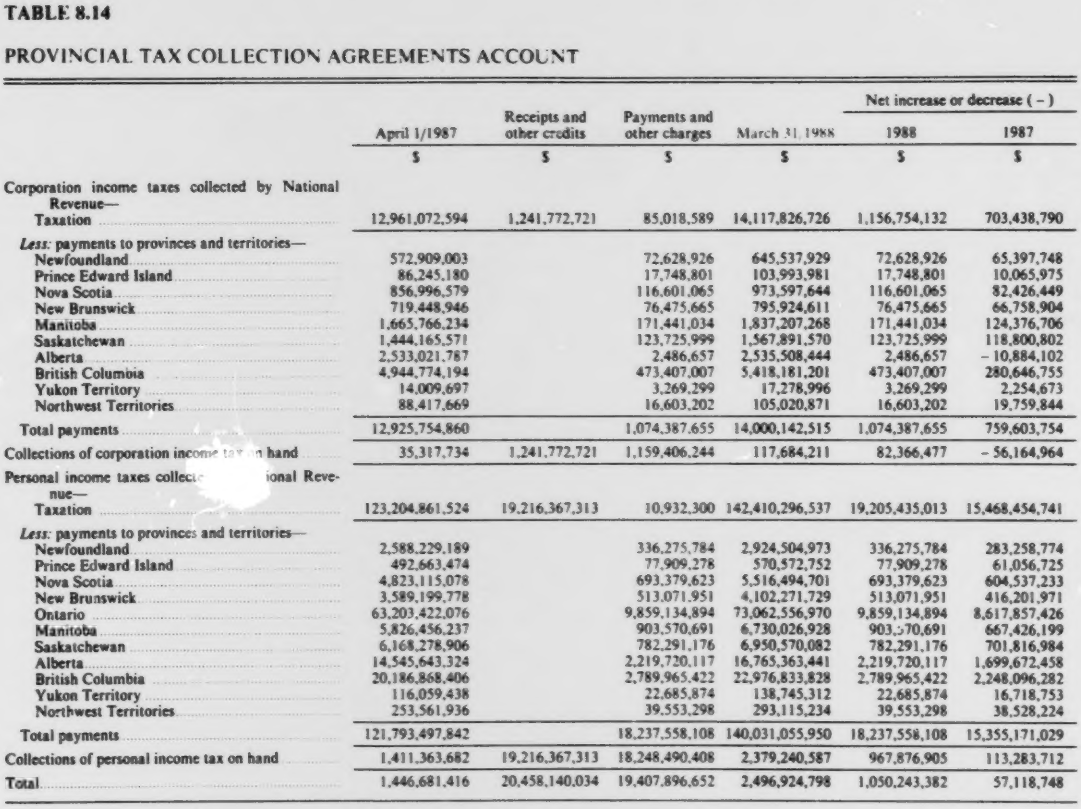

TABLE 8.14

PROVINCIAL TAX COLLECTION AGREEMENTS ACCOUNT

	April 1/1987	Receipts and other credits	Payments and other charges	March 31, 1988	Net increase or decrease (–) 1988	Net increase or decrease (–) 1987
	$	$	$	$	$	$
Corporation income taxes collected by National Revenue—						
Taxation	12,961,072,594	1,241,772,721	85,018,589	14,117,826,726	1,156,754,132	703,438,790
***Less:* payments to provinces and territories—**						
Newfoundland	572,909,003		72,628,926	645,537,929	72,628,926	65,397,748
Prince Edward Island	86,245,180		17,748,801	103,993,981	17,748,801	10,065,975
Nova Scotia	856,996,579		116,601,065	973,597,644	116,601,065	82,426,449
New Brunswick	719,448,946		76,475,665	795,924,611	76,475,665	66,758,904
Manitoba	1,665,766,234		171,441,034	1,837,207,268	171,441,034	124,376,706
Saskatchewan	1,444,165,571		123,725,999	1,567,891,570	123,725,999	118,800,802
Alberta	2,533,021,787		2,486,657	2,535,508,444	2,486,657	– 10,884,102
British Columbia	4,944,774,194		473,407,007	5,418,181,201	473,407,007	280,646,755
Yukon Territory	14,009,697		3,269,299	17,278,996	3,269,299	2,254,673
Northwest Territories	88,417,669		16,603,202	105,020,871	16,603,202	19,759,844
Total payments	12,925,754,860		1,074,387,655	14,000,142,515	1,074,387,655	759,603,754
Collections of corporation income tax on hand	35,317,734	1,241,772,721	1,159,406,244	117,684,211	82,366,477	– 56,164,964
Personal income taxes collec[illegible]ional Revenue—						
Taxation	123,204,861,524	19,216,367,313	10,932,300	142,410,296,537	19,205,435,013	15,468,454,741
***Less:* payments to provinces and territories—**						
Newfoundland	2,588,229,189		336,275,784	2,924,504,973	336,275,784	283,258,774
Prince Edward Island	492,663,474		77,909,278	570,572,752	77,909,278	61,056,725
Nova Scotia	4,823,115,078		693,379,623	5,516,494,701	693,379,623	604,537,233
New Brunswick	3,589,199,778		513,071,951	4,102,271,729	513,071,951	416,201,971
Ontario	63,203,422,076		9,859,134,894	73,062,556,970	9,859,134,894	8,617,857,426
Manitoba	5,826,456,237		903,570,691	6,730,026,928	903,570,691	667,426,199
Saskatchewan	6,168,278,906		782,291,176	6,950,570,082	782,291,176	701,816,984
Alberta	14,545,643,324		2,219,720,117	16,765,363,441	2,219,720,117	1,699,672,458
British Columbia	20,186,868,406		2,789,965,422	22,976,833,828	2,789,965,422	2,248,096,282
Yukon Territory	116,059,438		22,685,874	138,745,312	22,685,874	16,718,753
Northwest Territories	253,561,936		39,553,298	293,115,234	39,553,298	38,528,224
Total payments	121,793,497,842		18,237,558,108	140,031,055,950	18,237,558,108	15,355,171,029
Collections of personal income tax on hand	1,411,363,682	19,216,367,313	18,248,490,408	2,379,240,587	967,876,905	113,283,712
Total	1,446,681,416	20,458,140,034	19,407,896,652	2,496,924,798	1,050,243,382	57,118,748

The data provided to Parliament on Tax Collection Agreements are difficult to understand.

Source: Extract from Public Accounts of Canada, 1987-88.

Exhibit 14.2

14.32 In view of the importance of the tax collection agreements to the Canadian federal system, accountability and reporting to Parliament should be improved. Such reporting should include information on the nature of the agreements, the federal government objectives in respect of the agreements and the results achieved.

Management's Response: *As noted in the Auditor General's remarks preceding the recommendation, the Federal-Provincial Fiscal Arrangements and Federal Post-Secondary Education and Health Contributions Act does not require or provide for any ongoing reporting to Parliament. This Act is frequently amended, as recently as 1987, at which time Parliamentarians have an opportunity to review it, including the part authorizing the*

Minister to enter into Tax Collection Agreements with the provinces. Nonetheless, the Department of Finance will take steps to improve the information available to Parliament on the Tax Collection Agreements. One appropriate mechanism might be through the Main Estimates, in particular Part III of these estimates, as they relate to the Department of Finance.

The tax collection agreements are not up to date, and some tax measures are being administered without proper authority

14.33 A number of tax collection agreements are, in some respects, out of date. For example, the federal government administers eight tax credits for one province -- for which it charges an administrative fee -- but these are not part of the tax collection agreement with that province. Some of these credits were initiated as long ago as 1984.

14.34 It may be argued that, although the agreements have not been amended to include provincial tax credits, correspondence between the federal government and the provinces concerned has the same effect. However, the Federal-Provincial Fiscal Arrangements and Federal Post-Secondary Education and Health Contributions Act requires that amendments to the agreements can be made only with the approval of the Governor in Council.

14.35 The federal government charges an administrative fee for all provincial tax credits administered by it in accordance with a specified formula. When a credit is not included in the agreement, there is no authority for levying the fee.

14.36 The Department of Finance should, in co-operation with the provinces, ensure that the tax collection agreements are updated on a regular and timely basis and that activities under the agreements are supported by proper authority. The Department and the provinces are in the process of updating the agreements.

Management's response*: These are agreements between two parties, the federal government and a province or territory, and as such are the joint responsibility of these parties. All of the provincial income tax measures administered by the federal government, and the manner of their administration, including the levying of any administration fee, have been agreed to with the provinces, at least by exchange of letters. As has been noted by the Auditor General, the federal government and the provinces are in the process of formally amending the agreements themselves so as to make them as up-to-date as possible. This will continue to be done expeditiously as future changes occur.*

14.37 The flat rate taxes levied by Saskatchewan, Manitoba and Alberta contravene the provisions of their respective tax collection agreements. The agreements require that "... individual income tax shall be expressed as a constant percentage (in one or more half percentage points) of the federal tax payable...." (emphasis added). The flat rate taxes, on the other hand, are calculated by applying a fixed tax rate to net income or taxable income.

14.38 The Minister of Finance has categorized flat taxes as temporary experimental measures for the purposes of the tax collection agreements. However, in the case of one province, the flat tax has been in place since 1985 and constituted in 1987 about 25 percent of the Province's total individual tax revenue. If the Province were to eliminate the flat tax but raise the same tax revenue, it would need to adjust its provincial tax percentage applicable to the federal tax payable from the present 50 percent to 62.5 percent.

14.39 The Department of Finance should take steps to rectify the existing contravention of the tax collection agreements with Manitoba, Saskatchewan and Alberta, resulting from the imposition of the flat rate taxes.

Management's response: *The Minister of Finance is discussing the future of flat taxes with provinces.*

Reporting to the provinces is in accordance with the agreements and payments are made on a timely basis

14.40 We found that the reporting to the provinces was generally in accordance with the tax collection agreements. There are regular consultations between federal and provincial officials about the administration of the agreements. The Department of Finance provides the provinces with information on such matters as estimates of payments and fiscal and economic forecasts. The Department also issues the Statement of Income Taxes Payable to the Provinces and Territories at the end of the year, which is accompanied by the opinion of the Auditor General of Canada. We found that the Department is making payments to the provinces on a timely basis as called for in the agreements.

Procedures for estimating payments to the provinces could be strengthened

14.41 For a taxation year, the federal government makes regular payments to the provinces based on its estimate of the taxes to be assessed under the provincial income tax legislation. After the actual assessment data become available 15 months subsequent to the end of the taxation year, final settlement is made to clear any differences between the actual assessment data and the estimated data on the basis of which interim payments were made. In other words, the provinces are paid the correct amount in accordance with the actual assessment data upon final settlement. However, if the interim payments are low because of the underestimation of taxes to be assessed under the provincial income tax legislation, there is a cost to the provinces in terms of lost interest. Conversely, overestimation of payments has a cost to the federal government.

Methodology for estimating and allocating income taxes payable to provinces needs review.

14.42 Except for one year in the period from 1980 to 1987, there has been net underestimation of interim payments to the provinces, in some years in significant amounts (see Exhibit 14.3).

14.43 The underestimation of interim payments has, in large part, resulted from deficiencies in the methodology used. Two of these deficiencies related to the valuation of allowances for the provincial share of estimated income tax deductions made at source for which no personal tax returns will be filed, and of provincial income taxes to be assessed in the current year but pertaining to earlier taxation years. The underestimation of basic federal tax has also sometimes contributed to interim underpayments. The Department of Finance has recently taken steps to deal with the first two deficiencies. The effectiveness of these steps in resolving the problem will need to be monitored.

14.44 The underestimation or overestimation of interim payments can have a disproportionately high impact on individual provinces. Their significance relative to the total provincial income tax revenue is demonstrated in Exhibit 14.3. For example, in 1987 the highest underestimation of payments to a province as a percentage of income taxes remitted by the federal government was 9.1 percent to Ontario, amounting to $893 million, while the highest overestimation in that year was 7.3 percent to Alberta, amounting to $153 million.

14.45 The Department of Finance allocates the estimated taxes payable to individual provinces on the basis of historical data The data pertain to the proportionate shares of individual provinces of basic federal tax and corporate taxable income for the most recent

NET UNDERESTIMATION/(OVERESTIMATION) OF INTERIM PAYMENTS OF INCOME TAXES TO THE PROVINCES

Taxation Year	Net Amount of underestimation/ (overestimation) ($ 000s)	Net Amount as a percentage of total income taxes remitted to all provinces	Highest underestimation/ (overestimation) of interim payments to a province as a percentage of total income taxes remitted to it [1]	
			Underestimation	Overestimation
1980	$ 970,505	10.5	14.5	[2]
1981	728,738	6.9	15.2	[2]
1982	53,926	0.5	8.4	(3.2)
1983	(299,680)	(2.6)	4.2	(9.6)
1984	176,434	1.4	4.9	(6.4)
1985	476,751	3.3	6.3	(2.8)
1986	399,312	2.5	8.7	(7.3)
1987	850,908	4.5	9.1	(7.3)

1. Excluding Northwest Territories and Yukon
2. No province was overpaid.

Source: Calculations based on data from the Department of Finance

Exhibit 14.3

taxation year for which assessment has been completed. This is normally one year before the current taxation year for individual income tax and two years before for corporation income tax.

14.46 The use of historical data results in low interim payments to the provinces experiencing proportionately higher economic growth than in previous years, as was the case with Ontario recently and Alberta in the 1970s. Some provinces have informed us that, in addition to interest loss, less accurate allocations can adversely affect their fiscal planning process. The Department of Finance prepares regular forecasts of provincial economies which could possibly be taken into account to provide a better basis for allocating taxes payable to the provinces.

14.47 The Department of Finance should review its methodology for the estimation and allocation of income taxes payable to the provinces.

Management's response: *The Department of Finance continually reviews the methodology for the estimation and allocation of provincial income tax payable to the provinces. On an aggregate basis the annual forecast error since 1981 has been less than 5 percent. As noted by the Auditor General, the Department has taken steps recently to further improve the forecasts of provincial tax payable and the results will be monitored. Work is also under way on improving the forecast of the allocation across provinces of provincial tax payable.*

UNDERESTIMATION/(OVERESTIMATION) OF TAX COLLECTIONS ATTRIBUTABLE TO THE PROVINCES AT YEAR END

Year	Amount ($ 000s)
1980	$ 503,550
1981	338,685
1982	195,250
1983	(660,076)
1984	(331,269)
1985	246,174
1986	348,793
1987	(77,700)

Source: Calculation based on data from the Department of Finance.

Exhibit 14.4

There are weaknesses in the existing accounting practices and procedures related to the Provincial Tax Collection Agreements Account. This Account forms part of the financial statements of Canada

14.48 The Provincial Tax Collection Agreements Account, which is maintained strictly for Public Accounts purposes, shows the liability of the federal government at any particular time, arising from the administration of the agreements. An entry is made in the Account every month making a provision for the liability to the provinces based on an estimated portion of the collections attributable to them. The liability is reduced as actual payments are made to the provinces by the federal government.

14.49 In recent years there has been underestimation or overestimation of the provincial share of tax collections in the Provincial Tax Collection Agreements Account (See Exhibit 14.4). Such underestimation or overestimation has a corresponding impact on the measurement of the budgetary deficit of Canada.

14.50 The underestimation or overestimation of the provincial share of tax collections has not been large in recent years relative to total provincial taxes assessed. However, the underestimation or overestimation can be significant relative to the budgetary deficit of Canada, particularly when one considers the changes in deficit from one year to another.

14.51 Several factors contribute to the underestimation or overestimation of the provincial share of tax collections in the Account. Some of these factors are within the control of the federal government.

14.52 In estimating the provincial share of tax collections adjustments are made to the collections data for such elements as tax refunds and federal and provincial tax credits. The refunds and credits for the current year are estimated to equal the amounts for the previous year. This may not be an appropriate assumption, particularly when the tax structure is undergoing significant changes. Further, the timing of tax refunds for the previous year can be influenced by such factors as the timing of the assessment cycle by National Revenue - Taxation

14.53 The estimating of the provincial share of tax collections could be improved, at least in part, by using available forecasts. The Department of Finance prepares forecasts of the current year's refunds and federal tax credits, and it receives forecasts of the provincial credits from the provinces. These forecasts, which take into account the current situation particularly with respect to the tax base and rates, could provide a better basis for adjustment to the collections. We understand from the Department of Finance that it will examine the possibility of using forecasts of current year's refunds.

14.54 No one group within the government takes full responsibility for the Account as a whole. The Department of Finance only accepts responsibility for making debit entries to the Account for payments made to the provinces. The Department of Supply and Services makes credit entries to the Account for the estimated taxes collected on behalf of the provinces. Neither department takes responsibility for determining that the balance of the Account represents the best estimate of the liability to the provinces.

14.55 The Department of Finance should improve its methodology and procedures for estimating the provincial share of tax collections in the Provincial Tax Collection Agreements Account.

Management's response: *The report recognizes that the underestimation or overestimation of the provincial share of tax collections has not been large in recent years when compared to total provincial taxes assessed.*

The Auditor General feels that the estimation methodology could be improved by using current-year forecasts of refunds and tax credits. We feel that this suggestion is reasonable and, as noted in the report, will examine the possibility of changing the estimation methodology in this manner.

15

DEPARTMENT OF NATIONAL HEALTH AND WELFARE

Canada Assistance Plan

15

DEPARTMENT OF NATIONAL HEALTH AND WELFARE

Canada Assistance Plan

Main Points

15.1 Under the Canada Assistance Plan (CAP) the federal government shares 50 percent of the costs of eligible social service programs delivered by the provinces and territories. Federal payments were forecast at $4.5 billion for 1988-89 and a further $600 million is provided in tax transfers to the Province of Quebec (paragraph 15.6).

15.2 CAP expenditures are statutory and do not require annual parliamentary approval except for administrative costs. CAP is also open-ended; there is no ceiling on the amount of federal support that will be provided (15.10 and 15.11).

15.3 In our view, the documentation of monitoring and verification activities that we reviewed was not adequate to support the federal certification that costs reported by the provinces for federal cost sharing were eligible and in compliance with CAP agreements (15.23 to 15.55).

15.4 We noted considerable progress in two areas that we commented on in previous audits. The settlement of claims has been brought to a more current basis and program policies and procedures have been documented (15.56 to 15.60).

15.5 In our view, the lack of information regarding social programs funded by CAP continues to be a problem. Members of Parliament and CAP management are not receiving comprehensive and descriptive information about the impact of CAP. The annual report, required by law, has not been published since 1984-85. In our view, Part III of the Estimates can be improved significantly (15.61 to 15.83).

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DEPARTMENT OF NATIONAL HEALTH AND WELFARE

Canada Assistance Plan

Introduction

Background

The federal government spends $5.1 billion as its share of the Canada Assistance Plan

15.6 The Canada Assistance Plan (CAP) is Canada's largest federal-provincial shared-cost program. CAP shares in the cost to the provinces and territories of providing social assistance to persons in need, and welfare services to persons in need or likely to become in need if they do not receive such services. While the federal government specifies conditions for cost sharing, provincial governments are responsible for the design and delivery of programs to the public. Federal payments to the provinces under CAP were forecast to be $4.5 billion in 1988-89. An estimated additional $600 million was to be provided via tax transfers to the Province of Quebec.

15.7 The Canada Assistance Plan Act became effective 1 April 1966. The wording of the CAP Act respected the provinces' jurisdictional responsibility for social programs. That is, the federal role was created as a passive or reactive one, limited to supporting provincial programs by contributing toward their cost.

15.8 All ten provinces had signed agreements under Part I of the Act by August 1967. Part II of the Act provided for the cost sharing of social services to status Indians living on reserve. Part III made provision for sharing in the cost of work-activity programs. No agreements have ever been signed under Part II of the Act and Part III agreements account for only a small percentage of CAP expenditures.

15.9 The Department has defined the objective of CAP in the Estimates Part III as being,

> "To support the provision by provinces and territories of adequate assistance and institutional care programs for persons in need, and the provision by provinces and territories of welfare services programs which have as their objective the lessening, removal or prevention of the causes and effects of poverty, child neglect or dependence on public assistance."

Federal support is open-ended

15.10 CAP is an open-ended, shared-cost program. Open-ended means that there is no ceiling on the amount of federal financial support that will be provided. Canada will pay 50 percent of all provincial costs found to be eligible and shareable under the terms of the agreements.

15.11 CAP payments are statutory; that is, the spending authority is provided by the Act and does not require further parliamentary approval. Nonetheless, the forecast expenditures are included in the Estimates to provide Parliament with a more complete picture of spending plans. Operating expenditures for CAP, which are approved annually by Parliament, were forecast to be about $6 million in 1988-89, or roughly 0.1 percent of total expenditures. This included the salary costs associated with 104 person-years.

15.12 CAP expenditures relate to millions of individual transactions at the provincial and municipal levels generated through hundreds of eligible programs. There are roughly one million social assistance case files that account for approximately 70 percent of CAP expenditures. There are also 6,000 homes for special care and 5,600 welfare service agencies, all providing services to eligible persons.

Previous audits: some concerns have been addressed; other previously identified problems persist

15.13 We previously examined and reported on CAP in 1978, 1982 and 1985.

15.14 Some of the concerns raised in our earlier reports have been addressed. In particular, we found considerable progress in the settlement of final claims and the documentation of program policy and operating procedures. We observed, however, that problems persist in the verification of claims and the provision of program information.

Audit Scope

We concentrated on the federal administration and delivery of the Plan

15.15 Our audit concentrated on the federal administration and delivery of the Canada Assistance Plan, which is by far the largest activity managed by the Social Services Programs Branch. It accounts for 98 percent of expenditures and 36 percent of Branch person-years.

Monitoring and Verification of Compliance

The contribution agreement with each province specifies the conditions that are to be met

15.16 The legislated objective of CAP is to make contributions toward the costs of provincial programs. There is a contribution agreement in place with each province that provides for federal cost sharing of provincial programs if certain specified conditions are met. These conditions are:

(a) financial assistance must be provided to persons in need;

(b) provinces must agree that a period of residence in the province or in Canada will not be required as a condition of eligibility for assistance; and,

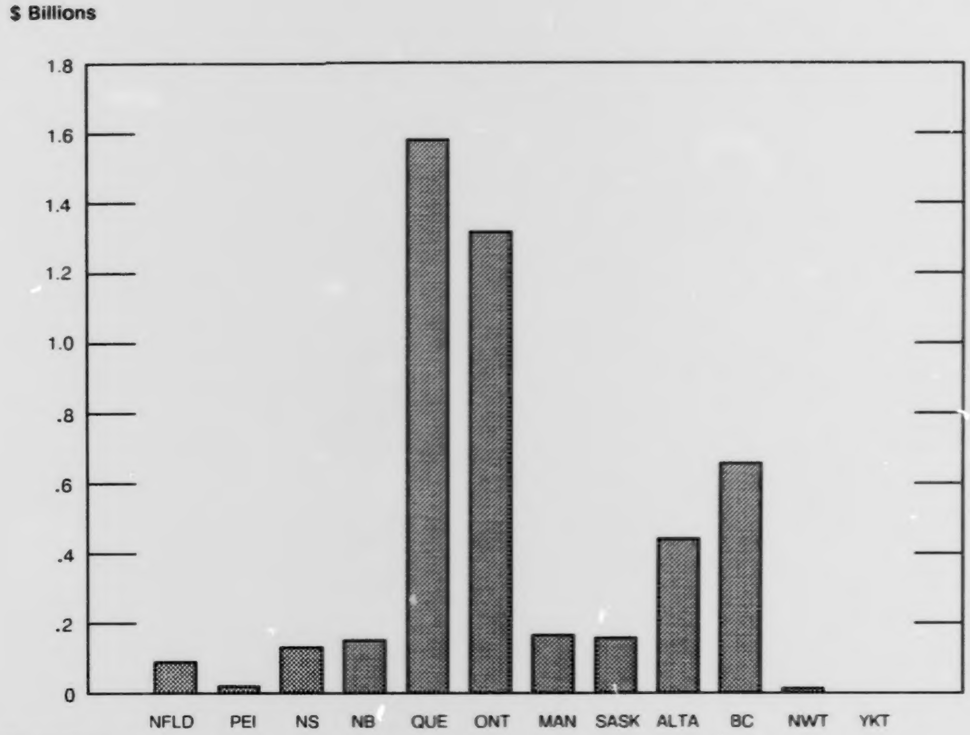
(c) provinces must establish, by law, a procedure for appeals from decisions with respect to social assistance.

Federal expenditures under the Canada Assistance Plan amounted to $5.1 billion in 1988-89. Our audit concentrated on the federal administration and delivery of the Plan.

CAP staff's main responsibility is to ensure that provinces conform with CAP agreements for purposes of cost sharing

15.17 Because the provincial governments are responsible for the design and delivery of programs, the main responsibility of CAP staff is to manage the contribution agreements by ensuring that provinces comply with the conditions for cost sharing and also that federal

FEDERAL CAP TRANSFERS
BY PROVINCE 1987-88



	NFLD	PEI	NS	NB	QUE	ONT	MAN	SASK	ALTA	BC	NWT	YKT
Percentage of Total Transfers	**1.9**	**0.5**	**2.7**	**3.2**	**33.4**	**27.9**	**3.5**	**3.3**	**9.4**	**13.8**	**0.3**	**0.1**

Source: Department of National Health and Welfare

Exhibit 15.1

obligations are carried out as required. Obligations to the provinces include the payment of contributions and making available statistical and other program information.

15.18 The 1989-90 Estimates Part III defines the federal responsibility for ensuring provincial compliance in more specific terms. "The main priority of headquarters and field staff is to determine shareability of provincial programs in accordance with the authorities. The second major activity relates to the review and audit of claims under CAP...."

15.19 CAP management monitors and verifies provincial compliance through the reviews by the CAP field operations staff on questions of eligibility and shareability, and by contracting for an audit of the accuracy of claimed costs.

15.20 Each month the provinces submit claims for cost sharing to the federal field offices. These are reviewed by the field office staff and submitted to headquarters for payment. Within a year or more after the end of the fiscal year, the provinces summarize the total shareable costs on a final claim, duly certified by the province and an auditor designated by the province.

15.21 The Federal Field Representative (FFR) then certifies that the final (summary) claim received "...represents fairly the eligible and shareable assistance and welfare services as provided in the Canada Assistance Plan Agreement". The accuracy of the costs on the final claim is verified by an audit at the federal level arranged for by CAP headquarters.

15.22 Any disagreements between the province and CAP headquarters over final claims are subject to negotiation. When agreement is reached, a letter, accompanied by a schedule, is forwarded to the province to confirm the adjustments. This finalization of a year's contributions is known as claims settlement.

Planning and Control

15.23 We observed weaknesses in the planning and documentation of monitoring and verification activities. In particular, we concluded that the Federal Field Representative's certification was not supported by the records and files we examined.

The planning process is incomplete

15.24 The planning process that supports the compliance activities is incomplete. There is no description of the overall planned approach showing, for example, how the review activities at provincial and federal levels combine to provide assurance that cost- sharing conditions are met. In the audit area, CAP management has now begun to work with some provinces to plan an improved approach to audit activities.

15.25 The Field Operations Division had a formal work-planning process in place during 1988-89. There are plans to have a Branch-wide planning process in place for 1989-90.

15.26 Monitoring and verification activities were not supported by performance measurement systems. There are plans to develop such systems during 1989-90 in conjunction with the revised work-planning process.

Conditions for Cost Sharing

We found instances of apparent non-compliance

15.27 As required, the final CAP claim and certificate signed and submitted annually by each province provides a general statement of compliance. None of the claims we examined noted any exceptions in terms of compliance.

15.28 Although our audit focussed on the federal administration of CAP, we did become aware of some instances of apparent non-compliance by provinces with the CAP Act. We found nothing to indicate how these instances were considered to be in compliance with the Act and the stated federal objectives of CAP.

Difficulties exist as to the definition of adequacy

15.29 Provinces can extend cost-shared social assistance to all persons in need, regardless of the cause of need. Individual eligibility is determined by the application of a provincial needs test that takes into account a person's net budgetary requirements. Provincial or municipal assistance rates are intended to provide for the basic requirements of the recipient.

15.30 The CAP Act does not specifically require that provincial assistance rates be adequate to provide for the basic requirements -- food, shelter, clothing, utilities, household supplies, and personal requirements. CAP cost shares assistance regardless of the level or adequacy of the rates. However, the objective of CAP calls for federal funding in support of adequate assistance.

15.31 A recent illustration of the complexity of assessing whether assistance rates are adequate to provide for basic requirements is the Finlay case. There the Federal Court of Canada ruled that CAP payments to a province were illegal so long as an allowance was reduced below the level of basic requirements as determined by the province in order to collect debts for overpayments. The federal government is appealing this ruling. The Department of Justice filed notice in the Federal Court of Appeal in April 1989.

15.32 We noted that in another province certain applicants could be provided with an amount less than the rate of assistance set by provincial law for basic requirements. This is normally done to encourage or discourage certain actions on the part of the recipient.

There are inconsistencies relating to residency requirements

15.33 Under the provisions of the CAP Act and agreements, a province shall not require a period of residence in the province to be a condition of eligibility for assistance. The intent of this provision is to ensure that persons in Canada who move from one province to another should have immediate access to assistance as required.

15.34 An exception to the Act has resulted from an understanding between the Department of National Health and Welfare and the Department of Indian Affairs and Northern Development that exempts provinces from applying the "no period of residence" condition to status Indians until they have established residency off reserve, usually for a period of 12 months. In one province, we found that municipalities also require applicants who are status Indians to prove that they were self-sufficient for that same period before qualifying for assistance. In that province the federal government, in effect, pays for almost the full cost of assistance to status Indians regardless of where they live.

15.35 In 1988, in our chapter on Indian Affairs, we reported that the Department made "...payments of approximately $50 million for social services to status Indians living off reserve who have not met provincial residency requirements for assistance". We were advised by CAP management that this did not result in a denial of assistance to anyone. However, if the arrangement regarding status Indians with provincial governments had not existed, the cost to the federal government would have been only $25 million, that is, 50 percent of the shareable costs.

15.36 Another instance of a residency restriction came to our attention. In that jurisdiction certain individuals may be required to have established residence for 12 months prior to application for assistance or have been employed there for 3 of the previous 12 months before applying for assistance.

15.37 The amounts involved in these instances may be small relative to total CAP payments. Nonetheless, we believe that where program delivery practices may be at odds with CAP legislation, they should be explicitly addressed either by enforcing the legislation or changing it, rather than by administrative policy.

15.38 Instances of possible non-compliance with the CAP Act should be investigated. The Act should be complied with, or amended if required.

Department's response: *The program does not, nor can it contest provincial interpretation of provincial legislation. This finding (paragraph 15.32) is based on an interpretation of provincial law by the Auditor General, different from that by the Province as explained to CAP officials.*

The Department is satisfied that it investigates areas of potential non-compliance, once it becomes aware of them, and that the investigations are appropriate to the circumstances in each case. The recommendation is overly simplistic as it recognizes neither the complexity of the legislation involved nor the difficulty of consistently applying its terms and conditions for sharing with twelve independent jurisdictions. The Department agrees with the Auditor General's comment that the amounts involved are not significant.

The outcome of appeals should be monitored

15.39 Provinces comply with the requirement to have an appeals procedure in place for social assistance cases. However, CAP field staff do not consistently monitor the outcomes of provincial appeal tribunals to determine whether rulings raise questions regarding compliance of provincial policy with the CAP Act. We also noted that some provinces had established limits on the appeals process. CAP management was concerned that these limits should not unduly restrict the application of appeal provisions in the CAP agreements. We were advised that CAP management intended to examine these limits to ensure that provinces were still in compliance with the CAP agreements.

Field Operations

15.40 The CAP Directorate maintains field offices in nine provincial capitals. These field offices are headed by a Federal Field Representative (FFR) supported by field officers and eligibility clerks. Their primary functions are federal/provincial liaison and the certification of provincial claims.

15.41 Claims certification, as outlined in a Field Operations Division December 1985 planning document, consists of the following activities:

- establishing that claims are shareable and that they are based on costs that can be identified in financial records, and
- verifying eligibility and shareability of amounts claimed.

There are shortcomings in the review process

15.42 Annual work plans are prepared by each of the FFRs. They describe the various review activities undertaken in support of the certification of provincial claims. The work plans are not based on an assessment of the relative value of the various types of review activities, or of the minimum amount of review required.

15.43 The review of social assistance case files is one of the claims certification activities. A sample of files is selected and reviewed to ensure that the recipient is eligible for and entitled to the benefit. The planning process does not require documentation of how the sample of case files is to be selected for review or how the number of files for review has been determined.

15.44 The actual number of files reviewed for 1988-89 in most regions was much lower than planned. By March 31, the end of the fiscal year, only 25 percent of the 24,475 planned case file reviews had been completed. In the previous year, 66 percent of the plan was accomplished. We found that neither the regions nor headquarters analyzed the cause or effect of this situation.

15.45 Some regions plan for field trips to various areas in their province. Others limit their review primarily to files located in the provincial capital. Planned trips are sometimes cancelled because of cuts to travel budgets. Changes to these planned review activities are not analyzed to determine the impact on eventual certification of the final claim. Most of the quarterly status reports that we reviewed did not provide explanations for variances from the review plan.

15.46 The review work performed by the field offices provides the support for certification of final claims. Although the written record of what work was done by the field staff varies from region to region, generally it does not fully show what tests were conducted. The records do not include information on determination of sample size, rationale for selection, or description of the tests performed.

Federal Audit of CAP

There is no national assessment of audit requirements

15.47 Audit is another part of the overall review effort directed at ensuring the propriety of provincial claims. Although review work by the federal field staff is carried out on an ongoing basis, the audit is conducted only after a final claim, certified by a provincial auditor, has been received for settlement. At present, CAP management does not rely fully on the opinion of provincial auditors with respect to the accuracy of costs or of their eligibility and shareability. As a result, CAP management contracts for a federal audit in the provinces and territories. The 1988-89 budget for audit was approximately $1 million.

15.48 There is no overall planning document that assesses audit requirements as a basis for developing the annual audit budget. Without this documented assessment, it is difficult to determine whether the amount of audit is too much or too little.

15.49 We found that CAP management has a well-documented process for the follow-up and resolution of audit findings.

New initiatives are underway

15.50 CAP management is working to better co-ordinate the different levels of audit that address the programs and costs claimable under CAP. For example, in one province, a public accounting firm conducts a review of claimed costs on behalf of a federal/provincial audit and settlement committee.

15.51 During the past few years, field operations staff have been developing a new approach for their review activities. This approach starts with a listing of all approved provincial programs and the identification of specific programs for detailed review by the FFR. The process improves on the current planning by clearly identifying the total population subject to review and by establishing review priorities.

15.52 We believe that the guidelines could be improved if they included reference to a process for co-ordination of audit and review at the federal or provincial level, and for appropriate reliance on this work. The guidelines could also specify what documentation staff performing reviews should include in their files as evidence of the work performed.

Recommendations Related to Monitoring and Verification

15.53 An overall planning document for monitoring and verification of compliance should be developed on a province-by-province basis. It should include an identification of audit and review activities at federal and provincial levels, and an assessment of the extent to which CAP can rely on the results of these reviews.

15.54 The nature, extent and timing of planned and actual review work should be documented.

15.55 Variations from annual review plans should be analyzed and the results used in updating the review plans.

Department's response: *Paragraph 15.21 does not adequately reflect the complete process. The FFR's certification is invariably accompanied by a long form report which notes exclusions from the overall certification, areas of concern to be covered through further verification process, and areas which require policy interpretation to be addressed through the issue resolution process.*

The Department does not contest the auditor's comment on the documentation of monitoring and verification processes. It does however consider that the planning of the process is complete in that it takes into consideration local conditions, problems, and opportunities and is aimed at providing a level of assurance consistent with the requirements of Central Agencies for the stewardship of federal contributions.

This report does not adequately reflect that the overall verification process leading to certification is effective. The Department accepts the comment and is now working to improve documentation.

Claims Settlement

There has been considerable progress toward achieving settlements on a timely basis

15.56 In the last two years there has been considerable progress in bringing settlements to a more current basis. The two largest provinces, however, are still considerably in arrears. As of 31 March 1989, Quebec was five years in arrears, and Ontario, seven. Until such time as settlement is reached, the payments to provinces continue to be in the nature of advances. However, we noted that when final settlements are reached, the adjustments required are relatively small when compared to total payments.

15.57 Issue resolution committees have been recently introduced in most provinces. These new federal/provincial committees are to resolve issues on a more timely basis, thereby keeping settlements more current.

Department's comments: *The Department has noted that this Report does not give, in its view, adequate recognition of the factors which have caused this result. The fact that required adjustments are relatively small, at time of final settlement, is directly attributable to the overall verification process which incorporates audit on behalf of CAP, audit on* *behalf of the provinces, work carried out by the federal field representatives and the work of the federal/provincial issue resolution committees.*

Manuals and Guidelines

Some progress: more work still to be done

15.58 Since 1978, when we first reported the need for documented procedures and guidelines, considerable progress has been made. These documents contain two types of instruction. They specify what activities are acceptable for cost sharing, as well as the procedures to be followed by CAP staff, primarily the field office staff.

15.59 At the end of our audit, the policy manual, which was to have been formally released in November 1985, had not yet been released to the provinces.

15.60 We found that there were no formal procedures in place for the revision and updating of manuals and guidelines.

A Lack of Information

15.61 The lack of information regarding social programs funded by CAP is a long-standing issue. Over the years there have been many studies and reports that recommended various actions to improve CAP-related information.

15.62 There has been limited action by CAP management to identify the information requirements of potential users of information about the operations and results of CAP, and to examine and meet their needs. For example, the information requirements of Members of Parliament (MPs) and the provinces (for national data) have not been defined.

Little information on program results

15.63 Comprehensive and descriptive information about the operations and impact of CAP is essential for informed consideration of this major federal program and its relation to other social security programs. However, MPs and others are not currently receiving such information.

15.64 Given the Department's stated objective for CAP, the most serious information gap may be the lack of information on program results. Why do individuals require assistance; how often; for how long? What programs have proved most or least effective in reducing reliance on welfare? Improved information regarding the causes, extent and effects of poverty and the impact of existing programs is necessary to evaluate the impact of federal cost sharing on Canada's social security system.

15.65 Because provinces design and deliver assistance and welfare services programs, it can be difficult for federal field staff to obtain information on the extent to which provincial programs achieve their stated objectives. However, the CAP agreement with each province provides that CAP management may request any information on the administration and operation of CAP that is practicable for the province to provide. This gives CAP management the right to an active role in obtaining information which could be used for planning and evaluation purposes. CAP management is now requesting such information under the CAP agreements to develop a national data base.

CHRONOLOGY OF INFORMATION RECOMMENDATIONS

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1965 A Reference Paper prepared by the Department of National Health and Welfare for a Federal-Provincial Welfare Ministers conference stated: "The advent of the Canada Assistance Plan emphasizes the need to re-examine the question of what statistics are needed, how they can be most effectively used in interpreting public assistance programs, and how they can contribute to a better understanding of, and hence more constructive action on, the causes, extent and effects of poverty".

1971 *Poverty in Canada*, Report of the Special Senate Committee on Poverty commented on the lack of adequate, authoritative data. Although their recommendation for the establishment of a Council for Applied Research goes beyond the capacity or mandate of CAP, they did point out the need for information that would contribute to a holistic framework for social policy in Canada.

1971 The Federal-Provincial Task Force on a Developmental Approach to Public Assistance and the Federal-Provincial Working Group on Costs of Welfare Programs made a number of recommendations including:

- that information systems within welfare programs provide data that will help to identify and define emerging social problems and support socio-economic planning;
- the appointment of a federal-provincial group of experts to develop an information system with common input and characteristics on welfare activities by each province and the country as a whole.

1981 The Parliamentary Task Force Report on Federal-Provincial Fiscal Arrangements: *Fiscal Federalism in Canada*. (Breau report), in a chapter on Social Assistance and Social Services: The Canada Assistance Plan recommended that:

- the Minister of National Health and Welfare undertake to review the extent to which provinces are meeting the Canada Assistance Plan conditions, and to consult with provincial colleagues on a more precise definition of the conditions.

It was also recommended that:

- the Canada Assistance Plan requirements for statistical and financial information be strengthened to improve understanding of the programs cost-shared under the Plan.

1985 The Study Team Report to the Task Force on Program Review: *Canada Assistance Plan* (Nielsen Task Force) in a synopsis of interviews conducted, noted that access to information is difficult for provinces and NGOs. Other comments included:

- there is a need for a better mechanism for federal provincial communication,
- there is a need for national standards and federal monitoring,
- there is a lack of national data collection on CAP.

1987 The National Council of Welfare (an advisory body to the Minister of Health and Welfare) in its report *Welfare in Canada: The Tangled Safety Net*, made 50 recommendations aimed at simplification, accessibility, equity, adequacy and due process including:

- that the provincial and federal government develop a set of consistent definitions and categories to describe social assistance caseloads and recipients, covering such aspects as demographic characteristics, type of assistance received and the length of time in receipt of assistance;
- that welfare statistics be made public at least on an annual basis in the form of both regular reports and additional research materials provided upon request.

1989 The Social Services Program Branch Working Group on Information Requirements noted that the information requirements of the Branch are not fully met by current data collection and analysis arrangements. The group recommended that a Branch-wide public information and communications strategy should be developed and implemented identifying the various publics' needs and how best to meet them.

Exhibit 15.2

15.66 Since its inception, no program evaluation of CAP has been carried out. In April 1989, an evaluation assessment report, prepared by the Department, recommended that a program evaluation of CAP be conducted. Following consultation with the provinces, agreement was reached to proceed with an evaluation study that is scheduled to be reported early in 1990.

Inadequate reporting

15.67 There is presently a lack of opportunity on an ongoing basis for MPs and others to review and consider the results of CAP. Part III of the Estimates should provide information on how dollars will be spent to achieve objectives, and on performance related to past spending. The annual report is intended to provide an opportunity for parliamentary review of CAP operations and payments under each of the agreements under the Act. Neither of these documents is accomplishing its intended purpose.

Estimates Part III: an opportunity for additional and fuller information

15.68 The reporting of the operations of CAP and its effects is incomplete. The federal government specifies conditions for cost sharing. Other than the review and audit of claims, Part III of the Estimates gives no indication how these conditions for cost sharing are monitored or the extent to which they are being met.

15.69 In June 1988, the Deputy Minister approved a new mandate for the Social Services Program Branch and its directorates, including CAP. The thrust is "to develop, promote and implement social welfare policies and programs which support and advance the well-being of the people of Canada." The program objective for CAP, as stated in the Estimates Part III, does not reflect this new proactive mandate.

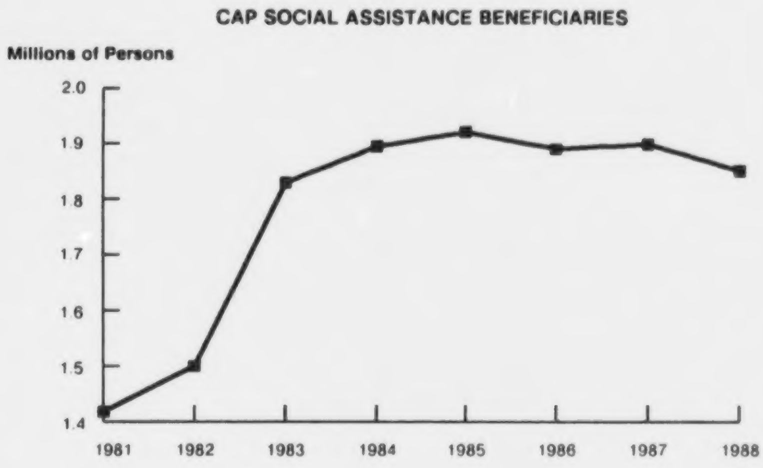
15.70 The impact of the statutory nature of CAP is not explained in Part III. The narrative material does not inform MPs that they are voting only the operating costs, which account for roughly 0.1 percent of CAP's total costs.

15.71 Our comparison of CAP Main Estimates and actual expenditures for 1983-84 to 1987-88 indicated that the projections of CAP expenditures for the last five years were fairly accurate (low of 1 percent and high of 4.7 percent variance).

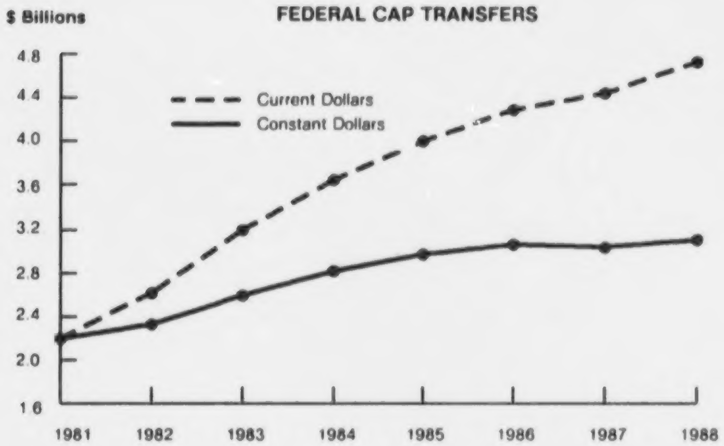
15.72 With respect to the number of individuals who benefit from CAP-funded programs, the Part III reports only order-of-magnitude information. The same figures have been reported for many years and give no indication of trends that may be developing in the recipient population. For example, the 1989-90 Part III reported "...assistance benefits to just over 2 million Canadians and welfare services to approximately 500,000 persons". These same figures appeared in the four previous Part III documents.

15.73 We believe that the presentation of additional information, such as trend data on the number of beneficiaries and poverty levels and comparative figures on assistance rates, would assist MPs in their consideration of program effectiveness. The Part III does not indicate where or how additional information may be obtained on CAP. Two examples of useful publications that could be referred to are the Inventory of Income Security Programs in Canada and Social Security Statistics. Both of these documents are produced by the Policy, Communications and Information Branch of the Department from information received from the provinces.

The number of CAP beneficiaries has remained quite stable since 1983. The growth in federal payments has resulted largely from increases in provincial social assistance rates.



Source: Statistics Canada



Source: Department of National Health and Welfare

Exhibit 15.3

Annual report: a requirement unfulfilled

15.74 The legislated requirement to produce a CAP annual report has not been met since 1984-85. It had been intended to do a 20th anniversary edition in 1985-86. At the time of our audit, it was not known whether, or when, an edition combining the missing years would be produced to comply with the legislated requirement.

15.75 In 1984-85, the annual report contained little more than the information provided in Part III of the Estimates. Earlier reports gave an overview of the income assistance and welfare services activities in each province as well as highlighting CAP activities for the period.

Problems with data collection

15.76 There are difficulties in collecting information. Federal/provincial program definitions are not harmonized and categories of recipients and beneficiaries are not consistent between provinces.

15.77 Also, turnover of clients is substantial with no mechanism to capture the number of individuals who actually benefit over the year. For example, the one million social assistance cases reported by CAP is at a specific point in time. This figure does not convey a sense of how many short-term recipients there may be throughout the year.

No national strategy: information is fragmented

15.78 Since the early 1970s, the Policy, Communications and Information Branch (PCIB) of the Department has funded up to 100 percent of provincial development costs for management information systems. In addition, CAP funds 50 percent of their computer-operating costs. PCIB contributions to date have totalled approximately $20 million.

> ***The nature of this kind of program limits the extent to which those at the federal level can be held accountable. Nonetheless, we believe that improved monitoring and verification by CAP management and better information on program results will help.***

15.79 Although CAP and PCIB have paid a large portion of the costs of these systems, there is no national strategy for data collection and usage in place. As a result, the data received from provinces is fragmented and difficult to roll up on a national basis. For example, there is no one set of categories common to all jurisdictions with respect to reasons for receiving social assistance.

15.80 Some information is available to CAP management through PCIB. For example, PCIB receives information from provinces that describes program objectives, eligibility criteria, and benefit types and levels. In addition, it receives statistical information on the demographics of provincial caseloads, depicting who the recipients and beneficiaries are -- for example, the disabled, the elderly, the unemployed, single parents, and children.

15.81 This information needs to be analyzed in order to provide a national picture of assistance and welfare services programs and beneficiaries. It could be included in the Estimates Part III, annual reports and other publicly-available documents.

Recommendations Related to Information and Reporting

15.82 CAP management should develop and report more comprehensive information on CAP-related activities and results.

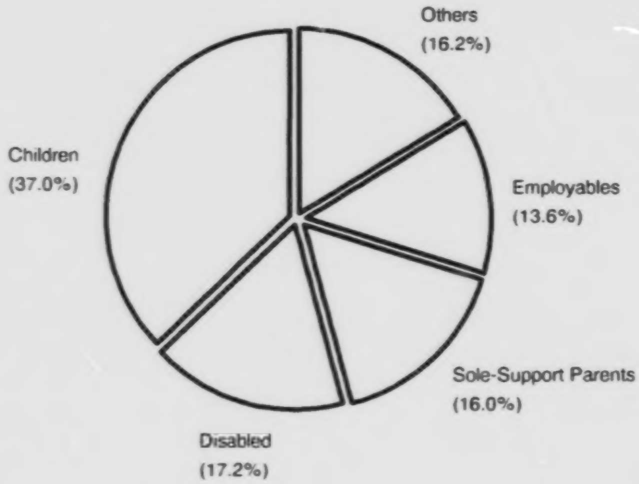
15.83 The CAP Annual Report should be prepared as required by law.

To Sum Up: Accountability is Difficult But Can be Improved

15.84 CAP was designed as a financial support program to make payments to the provinces to share in their costs for providing social assistance and welfare services. The very nature of this type of shared-cost program imposes some limits on the extent to which those administering it at the federal level can be held accountable for its overall costs, other than administrative costs, or its results.

Approximately 500,000 persons or 26 percent of Canada's social assistance beneficiaries live in Ontario. In 1987, their profile was as illustrated.

SOCIAL ASSISTANCE BENEFICIARIES IN ONTARIO, 1987



Source: Ontario Ministry of Community and Social Services as displayed in the Report of the Social Assistance Review Committee

Exhibit 15.4

15.85 Initiatives are underway to improve some aspects of CAP's administration. Some areas, particularly those relating to the monitoring of compliance and claims verification, can be further improved. We also believe that CAP management can play a more assertive role in information gathering, analysis, and reporting. We believe that this is essential if better accountability for $5.1 billion in federal expenditures is to be achieved.

16

QUALITY ASSURANCE

16

QUALITY ASSURANCE

Main Points

16.1 The Government of Canada spends more than five billion dollars annually on a variety of products. To ensure the quality of these products it has traditionally relied on product standards, inspection and warranty. These methods have been adequate for low technology and high volume production, but appear to be inadequate when dealing with higher technology and complex products that require a more comprehensive approach to quality assurance (paragraphs 16.7 and 16.19).

16.2 More is at stake than the quality of the products themselves. In a number of cases, we noted that deficiencies in quality assurance practices have had a detrimental effect on the operational efficiency of equipment purchased for government departments (16.36, 16.41, 16.47 and 16.52).

16.3 Since the 1960s, a more comprehensive approach, commonly known as "Quality Assurance", has been used by purchasers to require suppliers to ensure that quality is built into the product. National and international standards for quality assurance have been adopted as requirements by an increasing number of Canadian companies. However, the government has not developed a position on the use of these standards in government purchases. As a result, in may of the contracts we examined, DSS and its customer departments had no specified requirements for the suppliers' quality systems in the tender documents (16.22 and 16.23).

16.4 The government is the largest single purchaser of Canadian goods. Its position on issues related to quality assurance is critical to Canadian companies. The government can, through its procurement procedures, take positive steps to encourage a more rigorous approach to quality and thereby enhance the reputation and competitiveness of Canadian industry, both at home and in the international market (16.24).

16.5 DSS has not had a corporate focus on quality assurance since 1979 when the Quality Assurance Branch was dissolved. However, we noted that this functional responsibility has recently been assigned to the Canadian General Standards Board. The Board will be involved in the assessment and application of quality assurance standards (16.26 and 16.27).

16.6 Because the contracts we audited were limited and not randomly selected, government wide conclusions were not drawn based on the contracts examined. However, our examination of systems and procedures uncovered issues which need to be addressed if a full quality assurance program is to be instituted (16.15).

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Exhibits

16.1 Product Areas and Number of Contracts Examined

QUALITY ASSURANCE

Introduction

16.7 The Government of Canada spends more than five billion dollars annually on a variety of products. To ensure the quality of these products it has traditionally relied on product standards, inspection and warranty. These methods have worked well for goods involving low-technology and high-volume production.

16.8 Because today's products are becoming more complex, prudent purchasers are expected to participate in various stages of design and production, although traditionally these tasks have been the responsibility of suppliers (including manufacturers, contractors and assemblers). Through a specific program, commonly known as "Quality Assurance", the purchaser must first clearly specify his technical requirements (including the requirements for quality assurance) and select suppliers who can meet the specified requirements. Then the purchaser must monitor the supplier's quality assurance system and inspect the product to ensure that all contractual requirements are met.

16.9 Relying on inspection to identify faulty items at or near the end of the production process is costly. It takes time, effort and money to inspect the products and to correct identified deficiencies. In addition, there are costs for repair, maintenance, liability, etc. when the products fail to perform satisfactorily. Experience in the United States has shown that the costs of not "doing the right things right the first time" total over 20 percent of gross sales for manufacturing companies. These costs are included in the prices that customers pay.

16.10 More is at stake than the quality of the products themselves. Product quality can affect the efficiency of government services and the effectiveness of its programs. In addition, there are direct effects on the ability of Canadian industry to compete in an increasingly difficult international market where quality is becoming a major factor.

16.11 Today's customers demand quality. Recently, more and more Canadian companies have applied new methods to ensure consistent quality of their products to meet customer requirements. As the single largest purchaser of Canadian goods, the Government of Canada has an important leadership role to play in this pursuit of quality.

Audit Objective and Scope

16.12 The objective of our audit was to determine whether the quality assurance systems and practices in selected departments and contracts conformed with generally recognized national and international standards for quality assurance.

16.13 The Department of Supply and Services (DSS) has the legislative mandate for "assuring the quality of materiel". We reviewed the history of quality assurance development in DSS and the related policies and procedures the Department has established.

16.14 We also examined the quality assurance practices followed in 18 selected contracts for 10 identified product areas in DSS, the Royal Canadian Mounted Police (RCMP), the Departments of the Environment (DOE) and Transport (DOT), and the Canadian International Development Agency (CIDA). We first determined the existence and adequacy of quality assurance systems and procedures in related branches of the departments and agencies. We then assessed whether these systems and procedures had been followed in the 18 contracts we examined. We also reviewed the relationships between DSS and the customer departments in exercising quality assurance in the selected contracts.

16.15 The contracts (see Exhibit 16.1) represent a wide range of product types purchased for government programs -- from simple, traditional items to technically complex equipment needed for major Crown projects (projects over $100 million). Because the contracts we audited were relatively few and not randomly selected, we could not draw broad government-wide or department-wide conclusions. However, our examination of systems and procedures uncovered issues which need to be addressed if a full quality assurance program is to be instituted. We plan to do additional work, wherever appropriate, on quality assurance in procurement of both goods and services. This will be done as part of our comprehensive audits in the future.

16.16 Our audit findings are presented below under **Observations and Recommendations**. Under **Case Studies** we show some of the deficiencies in quality assurance found during our audit of the 18 contracts.

Observations and Recommendations

Inspection alone cannot always assure quality

16.17 **Quality assurance is more than inspection**. Inspection has traditionally been an important element in ensuring the quality of goods but, particularly since the 1960s, quality assurance is understood to encompass much more. DSS directives agree with definitions by national and international standards associations. These stipulate that, depending on the value and the nature of the product to be purchased, quality assurance includes some, often all, of the following actions:

- the proper definition of requirements and specifications;
- appropriate requirements for the supplier's quality assurance system;
- judicious sourcing and thorough evaluation of suppliers;
- proper quality assurance clauses in contract documents;
- surveillance of the supplier's quality assurance system;
- a specified level of product inspection; and
- formal feedback on product performance in service.

Product quality can affect the efficiency of government services and the effectiveness of its programs.

16.18 **Despite inspection there are quality deficiencies.** A 1986 DSS internal study revealed that, by and large, departments used inspection extensively to assure quality, and that this had failed to ensure consistent results. In our examination of the selected contracts, we confirmed that in many cases departments had continued to rely heavily on inspection for quality assurance.

16.19 We found that the inspection approach worked well for products involving low-technology and high-volume production, such as RCMP uniforms and ammunition, but inspection alone was not appropriate for more complex government purchases, such as airport emergency vehicles and satellite station equipment (see case studies for details).

PRODUCT AREAS AND NUMBER OF CONTRACTS EXAMINED

Department or Agency	Product Purchased	Technical Complexity *	No. of Contracts Examined
DSS	Modular Office Furniture	Low	2
RCMP	Uniforms	Low	1
RCMP	Ammunition	Low	1
DOE	Small Marine Craft	Low	3
DOE	Special Purpose Vehicles	Medium	4
DOT	Airport Emergency Vehicles	Medium	1
DOT	Buoy-handling Systems	Medium	1
DOT	Water Bombers	High	1
CIDA	Rail Equipment	Medium	2
CIDA	Satellite Ground Station Equipment	High	2
Total Number of Contracts			*18*

* **Low:** Standard items
Medium: Manufacture to government specifications
High: Design and manufacture to government specifications

Exhibit 16.1

We found that even when inspections were properly planned and carried out, product quality could still be unsatisfactory if other quality assurance deficiencies existed.

16.20 In the contracts we examined, quality problems stemmed from the supplier's lack of an adequate system for quality assurance. DSS and/or its customer departments had not specified requirements for the supplier's quality assurance system, had not evaluated the supplier's quality assurance capability before awarding the contract, or had not monitored the supplier's quality control system during the execution of the contract to ensure its effective functioning.

16.21 Standards for supplier's quality assurance are inadequate. DSS directives, and its customer manual on quality assurance, stipulate that requirements for a supplier's quality system should be considered under certain conditions, for example when a contract involves: a dollar value exceeding $10,000; product safety impact; newness of design; technical complexity; or past failure by the supplier to conform with specifications. All contracts we examined met one or more of the above conditions, but most did not contain specific requirements for suppliers' quality assurance. This could be attributed to the fact that specification of such requirements is not mandatory even under the prescribed conditions; customer departments lacked the expertise to specify the requirements; and DSS did not ensure that adequate requirements were specified in contract documents. Furthermore, procedures for selecting an appropriate level of quality assurance standards had not been developed by DSS.

16.22 In 1975 the Canadian Standards Association (CSA) published a series of quality assurance program standards -- consisting of four levels of increasingly stringent requirements. These CSA standards were developed by industry representatives using a consensus approach and were updated in 1979 and 1985. A guide for selecting and implementing quality assurance standards was published in 1986. The CSA standards and guide have been used by an increasing number of Canadian companies as the basis for their own quality assurance systems and as requirements with which their suppliers must comply. Since 1987, quality assurance standards developed by the International Standards Organization have also received increasing recognition internationally and are being adopted universally in Europe. In addition, more and more companies, both in Canada and abroad, now require that the quality assurance systems of their suppliers be subjected to third-party assessment and certification to a recognized standard prior to awarding a contract.

16.23 In 1984 a request by the Deputy Minister of DSS to investigate the potential use of CSA standards in government led to the internal study mentioned in paragraph 16.18. However, the task force did not specify the extent to which the CSA quality assurance standards should be applied to government purchases. As well, the government had not decided whether it should subject its suppliers to this independent certification.

16.24 Because the government is the largest single purchaser of Canadian goods, its position on issues related to requirements for suppliers' quality assurance systems will have a significant impact on Canadian industry. By promoting the importance of quality and by encouraging the use of quality assurance standards, the government, in concert with major industrial associations, could help increase the competitiveness of its suppliers in the market at home and abroad. The costs of improving quality systems in Canadian companies would be more than offset by the reduction in the amount of rejects, rework and warranty repairs.

[illegible] government can take [illegible] steps to encourage a [illegible] approach to [illegible]

16.25 DSS should consider, in consultation with central agencies, the clarification of government policy on requirements for suppliers' quality assurance systems, including the adoption of Canadian or international quality assurance standards and related independent assessment and certification. DSS should develop and promulgate procedures for selecting and specifying supplier quality assurance requirements.

DSS's response: *Supply and Services agrees that this is an area which should be further addressed, in consultation with central agencies and departments of government. The clarification of the government's policy on quality assurance systems for suppliers cannot be done in isolation from the supplier marketplace, nor can it be done in haste, and thus the department recognizes the need to involve industry in all sectors in a planned approach to the development of policy.*

There are systemic weaknesses

16.26 DSS had no corporate quality assurance focus. Through the Department of Supply and Services Act, Parliament has assigned to the Minister responsibility for purchasing and, explicitly, for "the assuring of quality of materiel". Until 1979 the Quality Assurance Branch of DSS administered a general quality assurance policy and published a series of directives. The Branch was dissolved in 1979 and the responsibility for quality assurance was distributed to the various DSS procurement branches.

16.27 The 1986 internal study by DSS found that this had contributed to many major deficiencies in quality assurance systems and practices. DSS formed a Product Quality Management Committee to implement the recommendations of the study. The Committee completed a public awareness campaign, provided training for procurement officers and amended quality assurance directives. However, a number of the study's key recommendations have not as yet been implemented.

16.28 In October 1988 the responsibility for the Committee was transferred to the Canadian General Standards Board (CGSB). The functional responsibility for quality assurance mandated to DSS was assigned to CGSB. CGSB has played an important role for some years in the development of standards and quality control. We were informed that this new corporate focus on quality assurance is being made to involve CGSB further in the assessment and application of the quality assurance standards. The line branches will be responsible for the application in the procurement process of the standards set by the CGSB.

16.29 **Departmental procedures and organization need to be strengthened.** Although DSS has been given statutory responsibility for quality assurance in the Government of Canada, in practice the funding department must share this responsibility with DSS. This is important to ensuring effective quality assurance and to establishing accountability for achieving it.

16.30 In the late 1970s, DSS signed Memoranda of Understanding (MOUs) with DOT and CIDA delegating to them its procurement responsibilities, including quality assurance, for certain products. We noted that these departments had not established appropriate quality assurance procedures and organizations to assume the delegated responsibility.

16.31 The 1978 DSS - DOT MOU was valid for one year but was never renewed. Of the three branches of the Department that we looked at, only Flight Services had maintained some quality assurance capability. In the other two branches, Airports Authority and Canadian Coast Guard, the division of responsibilities for quality assurance between DSS and DOT was not clear. In addition, we found that, although DOT technical people were involved in some quality assurance work, there were no written policies and procedures.

16.32 DOT should develop appropriate quality assurance policies and procedures for use by the Airports Authority and the Canadian Coast Guard branches.

***DOT's response**: The Department concurs with the recommendation. The Marine Group has already commenced development of quality assurance policies and procedures.*

16.33 The DSS - CIDA MOU was renegotiated in 1986. We found that the importance of product quality to the Agency's aid projects was well recognized. The president of CIDA started a campaign for quality improvement in 1987, but there was no Agency-wide policy on quality assurance and this functional responsibility had not been clearly assigned to a single organizational unit in CIDA. In addition, although quality assurance guidelines for procurement had been developed for Canadian executing agencies of CIDA projects, these procedures were not mandatory and did not cover contracts for which DSS or recipient countries assume purchasing authority.

16.34 CIDA should assign the functional responsibility for quality assurance to a senior Agency executive and charge him or her with developing and implementing an Agency-wide quality assurance policy and procedures to cover all CIDA-funded contracts.

***CIDA's response.** It is agreed that the Agency will consider the possibility of assigning the functional responsibility for Quality Assurance to a Senior Agency Executive. This can* *be more adequately considered subsequent to the establishment of an overall government policy on Quality Assurance.*

16.35 DSS should, in consultation with its customer departments, clarify and agree to an acceptable division of responsibilities for quality assurance. DSS and central agencies should provide policy and functional guidance on quality assurance to departments wherever necessary. DOT and CIDA should ensure that their policies and procedures are consistent with central policy and directives on quality assurance developed and issued by DSS and central agencies.

DSS's response: *The division of responsibilities between Supply and Services and customer departments is described in the Supply Policy Manual, and the DSS Customer Manual. As recently as 1988, the department revisited and re-articulated the division of responsibilities to clients through Deputy Minister communication. Nevertheless, the department is in a review process of the aforementioned document which will include consultation with client departments to determine if there are areas which require further expansion or clarification.*

CIDA's response: *DSS has the overall responsibility to establish a government policy on Quality Assurance applicable to all procurement projects. Subsequent to this policy being established, CIDA will prepare its own policy within the framework set by DSS for application to CIDA funded projects.*

DOT's response: *The Department supports the recommendation that consultation should be held to clarify the division of responsibilities with customer departments of DSS.*

CASE STUDIES

Case 1. Buoy-handling Systems for Coast Guard Ships

16.36 In 1983, the government entered into contracts with four shipyards to construct six Type 1100 ships for the Canadian Coast Guard (CCG) to be used for buoy tending and ice breaking. CCG selected a British design, "speedcrane", as the buoy-handling system. The shipyards subcontracted the work to a British firm, which in turn engaged a Canadian agent to construct the speedcranes, in order to meet the level of Canadian content required by the government.

16.37 A serious problem with the buoy-handling system for these ships was noted in our 1987 Report. We concluded at that time that the buoy-handling equipment did not meet specifications and required extensive modification.

16.38 In January 1988 CCG implemented a corrective action plan to carry out the necessary modifications, but the costs of the modification were substantial. For example, the refit and repair costs for the crane on one of the six ships exceeded $300,000. The vessel worked none of the 1278 workable hours available for the navigational aids program because its speedcrane was being modified (refer to Chapter 22 Department of Transport - Canadian Coast Guard - Protecting Mariners' and the Public Interest).

16.39 In addition to the corrective action plan, an internal review of the speedcrane system was carried out in 1988 at the request of CCG management, to determine what had gone wrong. The review revealed many factors that had contributed to the unsatisfactory result, several of them deficiencies in quality assurance practices. For instance, a Statement of Operational Requirements for the buoy-handling system had not been developed by CCG. As a result, there was no basis for the parties involved to assess the crane design. Furthermore, changes were made to the original speedcrane design to satisfy Canadian content requirements, without adequate analysis, testing and approval. The operational ability of the prototype design was not verified.

16.40 We found an anomaly in the sharing of quality assurance responsibilities between DOT and DSS. In 1978 a Memorandum of Understanding (MOU) was signed between DSS and DOT, delegating procurement responsibilities (including quality assurance) for technical products to DOT. The arrangement was not renewed after one year as had been stipulated in the MOU. Unlike other branches of the Department where the complete quality assurance process was handled by departmental officials, CCG relied on DSS to carry out inspection of speedcranes. This division of responsibility, in our opinion, contributed to the deficiencies in quality assurance practices noted by the internal review.

Case 2. Emergency Vehicles for Canadian Airports

16.41 In 1983 the Treasury Board approved a Department of Transport submission to procure a fleet of 68 airport emergency vehicles, at a total cost of approximately $22 million. These vehicles were intended to be the primary units for crash, fire-fighting and rescue services at airports owned and operated by DOT, to meet the airport safety standards of the International Civil Aviation Organization.

16.42 The specifications for the vehicles were developed by DOT and the responsibility for detailed design and construction was left with the contractor. DOT retained the right to approve a prototype. When the prototype was delivered for testing it was found to have several deviations from specification, which were eventually corrected and allowed production to proceed.

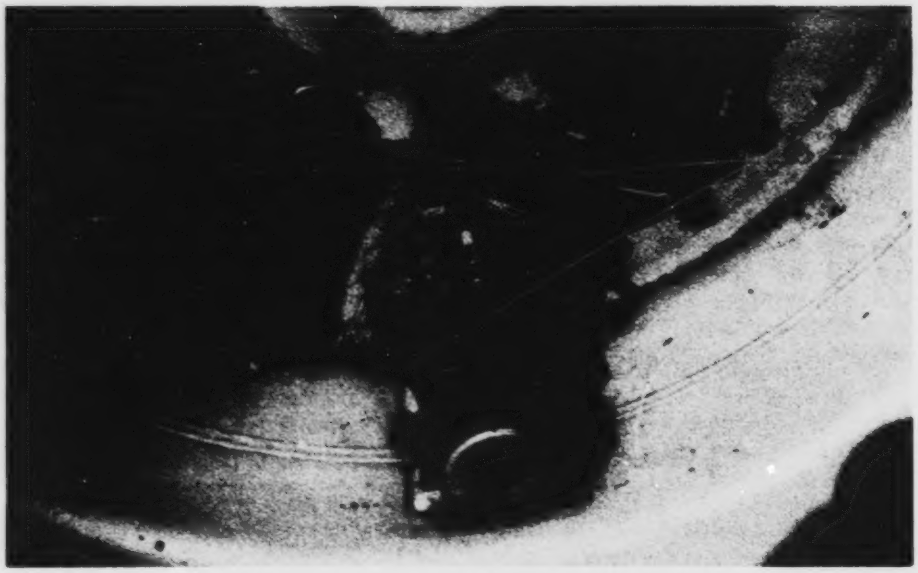
16.43 A requirement to establish an adequate quality assurance program was critical, given the size of the purchase, the newness of the design and the importance of emergency operations. Nevertheless, this requirement was not specified in the contract, nor was the manufacturer's existing quality assurance system verified by the department.

16.44 Departmental documentation indicates that DOT inspectors noticed deficiencies in the vehicles delivered for acceptance testing and were concerned therefore about the contractor's quality assurance system. The contractor reinforced its inspection system but was unable to satisfy DOT. The number of deficiencies reported by DOT, and the fact that their deficiencies were dealt with at the final inspection point resulted in increased time and cost being incurred during the acceptance process for both the manufacturer and the department. In the final analysis all 68 vehicles were accepted by DOT.

16.45 Acceptance tests cannot, and are not designed to, identify all defects. Although the deficiencies reported by DOT inspectors were rectified by the contractor before the vehicles were accepted, many other deficiencies surfaced after delivery. In a survey conducted by DOT soon after all vehicles had been delivered, 21 were reported to have various operational problems with the central tire deflation system (CTDS). CTDS, which costs more than $30,000 per vehicle, is a critical feature specified by the DOT design authority, to provide the emergency vehicles with additional traction for operating in difficult terrain. The prime contractor agrees with the assessment of the CTDS system and notes that DOT was informed of possible serious operational problems in April 1987.

16.46 We were also informed by the vehicle operators that problems continue with the computerized instrument display system and with the transmission.

The central tire deflation system (CTDS) on this vehicle has been removed for repair. CTDS is a feature for emergency vehicles which assists them to operate in difficult terrain (see paragraph 16.45).



Case 3. Satellite Ground Station Upgrade for Bangladesh

16.47 A satellite ground station in Bangladesh was constructed in 1975 with CIDA funding, to be the key telecommunications link between Bangladesh and the rest of the world. It was upgraded in 1983 through local funding and again in 1986 under CIDA funding. Both upgrades were contracted to the original supplier. The focus of our audit was the 1986 upgrade, funded at a cost of $2.8 million through a Memorandum of Understanding on Agro-Industrial Support Program (MOU-AISP), signed in 1983 by Canada and Bangladesh.

16.48 Under the MOU-AISP arrangement, Canada delegated purchasing authority to Bangladesh. Although the contract was signed between the Bangladesh government and the Canadian supplier, CIDA was accountable for the funds expended on this project. The MOU-AISP recognized the need for consultant services to assist the Bangladesh government in procurement activities. CIDA engaged a number of technical consultants to assist in preparation of specifications, inspections, acceptance tests, training and project monitoring.

16.49 However, the requirement for the contractor to establish and maintain an adequate quality assurance system, which would normally be stipulated in procurement of this kind of complex equipment, was not specified in the Bangladesh contract. Instead, CIDA relied on the contractor's own quality assurance system and the provision of warranty. Furthermore, the CIDA project monitor attended all major in-plant tests as well as field commissioning and while he reported deficiencies to CIDA, he did not have direct authority to initiate corrective action.

16.50 Several unusable parts were shipped to the project site and a number of system modules failed during the on-site acceptance tests. During our inspection of the site three months after the acceptance tests, many deficiencies remained. A major sub-system was not operational, due to defective parts and water damage during transit. Since then, many of the deficiencies have been corrected by the use of spares. However, faulty components that were returned to the contractor for repair or replacement under warranty have not yet been shipped back to Bangladesh. This delay was due to an ongoing contract dispute.

Quality assurance deficiencies contributed to the delay in the full operation of this Bangladesh satellite ground station (see paragraph 16.51).

16.51 During our examination we also noted that the station was operating under a waiver on the antenna system, issued by the International Telecommunication Satellite (INTELSAT) after the 1983 upgrade. This CIDA contract was not meant to address antenna problems related to the waiver. However, if the station's antenna deteriorates further and causes interference with other stations, it could be shut down by INTELSAT, in effect cutting off satellite communication in Bangladesh.

Case 4. Purchase of Railcars for Senegal

16.52 In 1986 CIDA purchased, on a sole source basis through DSS, 100 railcars for Senegal from a Canadian rail equipment company, at a cost of $8.3 million.

16.53 Railway development has been a major focal point for CIDA in its aid program. An internal evaluation of the Railway Aid Program, completed in 1986, found that Canadian rail equipment supplied by CIDA to foreign operations had a shorter life than its normal design life. The evaluation identified several quality deficiencies, such as non-conformance to specifications and defects in the original design. It suggested that responsibility for the problem rested jointly with CIDA, the recipient countries and Canadian suppliers.

16.54 For this project, a requirement for supplier quality assurance was specified in the contract. Although the company had developed a quality assurance manual, it had not implemented the program at the time of the contract. Recognizing this shortcoming and given the urgency of the contract, CIDA engaged technical consultants to carry out inspections, as had been its practice previously.

16.55 During in-plant inspections, inspectors hired by CIDA found numerous defects and welding deficiencies in the railcars and recommended a review of the company's quality control procedures. All the defects found by the inspectors were subsequently rectified before the cars were shipped to Senegal.

16.56 As part of the corrective action, the company and CIDA agreed that a field inspection would be performed after the railcars had been in service for approximately a year, to determine whether the corrective measures taken had been adequate. The planned inspection had not been carried out more than 24 months after delivery of the railcars. We were informed by CIDA that this inspection would take place before January 1990.

Case 5. Contracts with Appropriate Quality Assurance Practices

16.57 Based on our examination of the selected contracts, we have concluded that quality assurance procedures in procuring modular office furniture by DSS, uniforms and ammunition by RCMP, and water bombers by DOT have been adequate. Some of the reasons for this, we found, are:

- Responsibility for quality assurance for the product is clearly assigned, either formally or informally. For example, the contract between DSS and the water bomber supplier specified DOT as the quality assurance authority. The quality assurance responsibility for uniforms and ammunition has traditionally been assumed by RCMP, with informal agreement by DSS. Modular office furniture is one of the stocked items for which DSS retains the procurement and quality assurance responsibility.

- In each of these product areas, the department involved has established and maintained a technical and quality assurance capability. Appropriate quality assurance policies and procedures have also been developed.

16.58 DSS and the respective customer departments have been able to maintain a co-operative, professional working relationship with suppliers.

17

FEDERAL REGULATORY REVIEW PROCESS

17

FEDERAL REGULATORY REVIEW PROCESS

Main Points

17.1 Regulations are important and pervasive instruments of national and international policy. In 1985-86, regulatory programs cost the government an estimated $2.7 billion and Canadians about $30 billion (paragraphs 17.4 and 17.6).

17.2 In 1986, the government implemented new administrative procedures for developing regulations, requiring ministerial and public servant accountability, full public participation, impact assessments of regulations, public disclosure of key information and periodic review of regulatory programs (17.11).

17.3 In our opinion, the government's new procedures for developing regulations support essential elements of public sector accountability. Our audit of the extent to which branches of four departments comply with the procedures found that (17.35 to 17.46):

- Accountability for the development of regulations is, for the most part, clear.
- Major improvements are needed in the public reporting of key information on regulations such as significant commercial benefits to private sector firms and costs to the government.
- Departments do not always provide all interested parties equal and consistent opportunities for consultation on proposed regulations.
- Departmental studies, at times, do not use the same approach to assessing benefits and costs of proposed regulations. A lack of a consistent approach can make some regulations appear to have higher benefits or costs than others.
- Departmental evaluations of regulatory programs need to be improved.
- In some cases, practical alternatives to a proposed regulation were not identified and assessed.
- The work of the Standing Joint Committee for the Scrutiny of Regulations is essential for maintaining Parliamentary control over regulation-making powers delegated to the government by Parliament.

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Exhibit

17.1 The Federal Regulatory Review Process

FEDERAL REGULATORY REVIEW PROCESS

Introduction and Background

17.4 **Regulations are important and pervasive instruments of national and international policy.** At the end of 1988, about 360 statutes were identified as being in force in the 1985 Revised Statutes of Canada. It is commonplace for Parliament to delegate to Cabinet its power to make certain laws within the framework of these Acts. These laws are often referred to as delegated legislation or regulations. Like legislation, they confer legally enforceable rights and impose legally enforceable obligations on citizens.

17.5 About 2,800 regulations approved by Cabinet or by individual ministers are listed in the Consolidated Index of Statutory Instruments. Their objectives range from protecting Canadians from threats to health and safety and from unfair business practices, to implementing international agreements which affect Canada's economy and environment. The Montreal Protocol for reducing the use of ozone-depleting chemicals, and the Canada-United States Free Trade Agreement, are examples of international commitments being extensively implemented through regulation.

17.6 In addressing areas critical to the Canadian public interest, regulations also impose significant costs. The 1985 Ministerial Task Force on Program Review (Nielsen Task Force) identified 146 federal regulatory and regulatory-related programs. The Review estimated that in 1985-86 the programs involved 34,500 persons and cost the government, including compliance monitoring and inspection, an estimated $2.7 billion. Canadians, according to the Review, paid hidden costs estimated to be at least $30 billion annually.

17.7 Broad reviews of regulatory programs and reform have been conducted, in 1980 by a Special House of Commons Committee and in 1985 by the Nielsen Task Force. One of the elements examined was the government's process for developing and approving regulations. In 1986, the government implemented new government-wide administrative procedures for developing and approving regulations. Our audit focused on the extent to which branches of four departments had complied with the government's administrative policy.

17.8 The findings of the House of Commons Committee and the Nielsen Task Force which focus on the regulatory process are outlined below. These findings provide a historical context for our conclusions and recommendations.

17.9 **The 1980 report of the Special House of Commons Committee recommended improvements to the regulatory process. These included:**

- strongly endorsing the principle of consultation, noting that early consultation is a fundamental feature of regulatory reform.
- stressing the importance of a disciplined approach to decision-making and recommending that all proposed regulations be subjected to an appropriate impact assessment, including consideration of such basic questions as: What is the problem? What alternative solutions have been considered? How will the proposal help? What are its drawbacks and advantages? Who will gain and who will lose? Why is regulation the best means of dealing with the problem?
- recommending that alternative solutions, "include policy instrument alternatives other than regulations such as taxes or subsidies, not simply alternative levels or standards of regulation."

- recommending that departments and agencies ensure that all their regulatory activities are evaluated periodically.

17.10 The 1985 Nielsen Task Force found problems with the federal regulatory process:

- There was "not a federal regulatory 'system' *per se*." There was "a largely unstructured, uncontrolled, highly variable, and thoroughly confusing mixture of legal requirements, policy guidelines, and ad hoc administrative practices."

- The government had "no effective mechanism to plan or control, on an overall basis, federal regulatory intervention in the private sector."

- There was "a multiplicity of arrangements for developing, approving, and implementing regulation. The combination of inconsistent policies and procedures from department to department...seriously detract from the efficiency, effectiveness, and fairness of federal regulation."

- Arrangements for private sector consultation were inadequate. "Federal consultation on proposed regulatory intervention was seen as uneven and inconsistent...There is no encouragement of procedures and approaches by regulators designed to ensure that all interests have a reasonable opportunity for participation and involvement in the regulatory process."

- The Socio-Economic Impact Assessment process was "inadequate, poorly supported and appears to be largely ignored."

- The government did not "have an effective mechanism for systematically evaluating existing regulatory programs and for deciding whether to continue, abolish or modify them."

17.11 The government's new administrative procedures, implemented in 1986, sought to address problems in the regulatory process. The principles underlying the procedures are stated in the **Guiding Principles of the Regulatory Policy** and the **Citizens' Code of Regulatory Fairness**. The major elements are:

- clear accountability of ministers and officials for regulatory actions;

- full opportunity for public consultation and participation in the regulatory process;

- an assessment of proposed regulations to ensure that benefits clearly exceed costs;

- clear and reliable public information on regulatory requirements and why they have been adopted;

- evaluation of the effectiveness of regulatory programs; and

- a secure foundation in law for actions of regulatory authorities.

17.12 The Regulatory Affairs Branch (RAB) of the Office of Privatization and Regulatory Affairs (OPRA) was established to help implement the administrative policy. Its objective is to promote public access to and involvement in the regulatory process. RAB is responsible for developing policies and procedures for the federal regulatory process, notably **The Federal Regulatory Process: Documents and Guidelines**. Its role is to co-ordinate regulatory action, exercise a service and challenge function, review departmental regulatory proposals to ensure that they meet the government's regulatory policies and advise its

Minister on the proposals. The Minister is a member of the special cabinet committee that approves the proposals.

17.13 **How the new Federal Regulatory Process is supposed to work:** Departments and agencies are responsible for developing regulations permitted by the legislation they administer. They are also responsible for consulting widely on the proposals. The regulatory process, illustrated in Exhibit 17.1, is described below.

17.14 To ensure that interested parties are aware of regulatory proposals, the government requires that early notice of an intention to regulate be published in the annual Federal Regulatory Plan. The information required in the 1988 and 1989 Plans included a description of the proposed regulation, anticipated impacts, statutory authority for the regulation, expected date of publication in the Canada Gazette and the departmental staff person to contact for further information.

17.15 Before and after notification in the Annual Federal Regulatory Plan, departments and agencies are expected to consult with interested parties. They are also expected to conduct impact assessments of not only proposed regulations but also alternatives to regulation such as subsidies, taxes and consensus standards.

Like legislation, regulations confer legally enforceable rights and impose legally enforceable obligations on citizens.

17.16 To proceed further, a department or agency is required to obtain cabinet approval for prepublishing the regulation and a Regulatory Impact Analysis Statement (RIAS) in Part I of the Canada Gazette. Prepublication is intended to allow for further comment and review by interested parties.

17.17 The RIAS is expected to contain information on why the proposed regulation is necessary, how it conforms with the government's regulatory policy, who was consulted and what their views were, what alternatives were considered and how the department intends to monitor compliance.

17.18 The RIAS process recognizes that regulations have benefits and costs to society as a whole as well as to specific sectors such as small business, and regional and environmental interests. It therefore requires that benefits and costs be assessed and "winners" and "losers" identified.

17.19 The policy allows for confidential information, such as commercially-sensitive data, to be protected from public disclosure.

17.20 The crucial function of the RIAS is to provide:

- Ministers with the information they require to make sound regulatory decisions; and
- the public with detailed information on federal regulatory proposals.

17.21 Before a regulation is submitted to Cabinet for prepublication approval, the RIAS is reviewed by RAB and the legal aspects of the regulation are reviewed by the Privy Council Section of the Department of Justice (PCOJ).

17.22 PCOJ's role is to review the regulation to ensure that it meets the requirements of section 3 of the Statutory Instruments Act; for example, that the regulation is authorized by statute and does not violate the Canadian Charter of Rights and Freedoms.

17.23 The prepublication phase normally lasts a minimum of thirty days. Based on any comments it receives, a department may either revise the proposed regulation or request

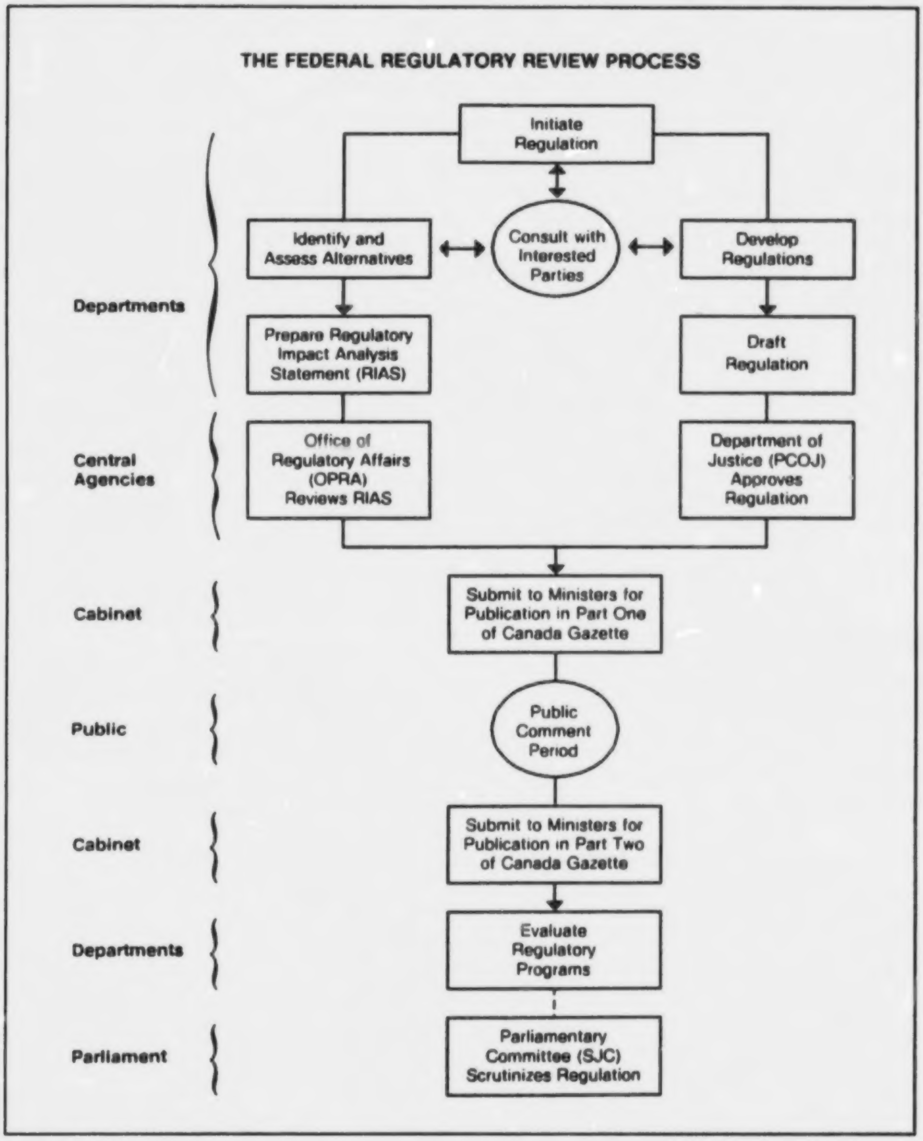
THE FEDERAL REGULATORY REVIEW PROCESS
Departments
Central Agencies
Cabinet
Public
Cabinet
Departments
Parliament
Initiate Regulation
Identify and Assess Alternatives
Consult with Interested Parties
Develop Regulations
Prepare Regulatory Impact Analysis Statement (RIAS)
Draft Regulation
Office of Regulatory Affairs (OPRA) Reviews RIAS
Department of Justice (PCOJ) Approves Regulation
Submit to Ministers for Publication in Part One of Canada Gazette
Public Comment Period
Submit to Ministers for Publication in Part Two of Canada Gazette
Evaluate Regulatory Programs
Parliamentary Committee (SJC) Scrutinizes Regulation

Exhibit 17.1

final approval by Cabinet for publication in Part II of the Canada Gazette. Once approved by Cabinet or individual ministers and registered, the regulation becomes law, but it is not normally enforceable until published in Part II of the Gazette.

17.24 The policy contains provisions for exempting regulations from prepublication; Cabinet must approve all exemptions.

17.25 Finally, the administrative policy requires that departments evaluate regulatory programs on a seven year cycle. Evaluations are undertaken by departments subject to technical guidance and quality control by the Office of the Comptroller General.

17.26 A Standing Committee of the Senate and the House of Commons reviews enacted regulations. The 1969 Report of the Special Committee on Statutory Instruments to the House of Commons recommended that a Standing Committee be established to review regulations. It based its recommendation on the principle that "parliamentary democracy is a system of government that requires the executive to be responsible to the legislature and that both be accountable to the people, and that there can be neither responsibility nor accountability where there is no knowledge of what has been done."

17.27 The 1969 Report led to the establishment of the Standing Joint Committee of the Senate and of the House of Commons for the Scrutiny of Regulations (SJC). The Committee is authorized to scrutinize all regulations after they have been approved by Cabinet or individual ministers. For example, regulations are reviewed to ensure that they are authorized by legislation, conform to the Canadian Charter of Rights and Freedoms, do not impose a charge, fine or penalty without legislative authority and do not trespass unduly on rights and liberties. The Committee recommends changes to regulations that it concludes do not conform to these criteria.

Scope - Special Audit

17.28 We conducted a special audit to determine the extent to which selected branches of four departments complied with the new regulatory process. Our audit included the Environmental Protection Directorate of Environment Canada; the Canadian Coast Guard, Transport Canada; the Occupational Health and Safety Branch, Labour Canada; and the Bureau of Radiation and Medical Devices, Health and Welfare Canada. We audited the process each used to develop regulations and reviewed recent regulations that had passed at least through the impact assessment phase. We reviewed the adequacy of consultation, the technical quality of impact assessments, the completeness of information provided to interested parties and the evaluation of regulatory programs. We also noted whether legal issues raised by the SJC were being resolved in a timely manner. For the most part our audit criteria were based on the requirements of the government's regulatory process. We developed additional criteria where needed.

17.29 We did not review the cost-effectiveness of the programs or the adequacy of regulatory compliance and enforcement.

17.30 A Special Audit covers matters that cut across government departments. By auditing several departments, the objective of a special audit is to identify significant problems which require further audit by this Office or review by the government and Parliament. It is not designed to allow a government-wide conclusion.

Major Findings

17.31 In our opinion, the Office of Privatization and Regulatory Affairs' (OPRA) 1986 administrative procedures for developing regulations identifies and supports essential principles of public sector accountability. Notably these principles include requirements for:

- clear ministerial and public servant accountability;
- early and extensive public consultation;

- reliable impact assessments;

- full public disclosure of information, including information provided to Cabinet, to interested parties; and,

- effectiveness evaluation.

17.32 It is especially noteworthy that the government's policy imposes an obligation on departments to disclose key information rather than requiring interested parties to search for it.

17.33 In adopting this administrative policy for regulations, the government has not only set out principles of accountability but also the criteria against which the performance of departments can be assessed. In this regard the approach is a model framework for public sector accountability.

17.34 Our overall conclusions on the extent to which the branches of the four departments we audited comply with these procedures are reported below.

17.35 **Accountability for processing regulations is, for the most part, clear.** Improvements are, however, needed in some of the departments in documenting roles and responsibilities of officials, specifying clear development milestones and tracking the status of regulations against the milestones.

17.36 **Consultation policies are generally satisfactory, but the actual process of consultation is not always adequate.** We found instances where interested parties were given ample opportunity to comment on proposed regulations. However, we also found situations where opportunities for consultation were unequal and inconsistent prior to publication of the proposed regulation in Part I of the Canada Gazette. In such cases, the views of commercial interests tended to be solicited earlier and more actively than those of "public interest" groups.

17.37 **Impact assessments of proposed regulations need to be strengthened.** The regulatory policy emphasizes the need for departments to identify and assess practical alternatives to regulation, for example, self-regulation. It also requires an examination of such options as various degrees of formal regulation, for example, different levels of control over emissions of pollutants. We found that assessments of alternatives to regulation were not always conducted and that assessments of proposed regulations sometimes did not include comparisons to other regulatory options. This approach reduces the usefulness of the analyses by not providing for the comparison of a proposed regulation with other practical regulatory and non-regulatory alternatives.

17.38 Comparability of impact assessments between departments is made difficult by the inclusion of different benefits and costs in departmental studies. One department included monetary estimates of the value of lives saved by regulations while others chose not to use such an estimate. Another department did not include estimates of commercial benefits to private sector firms or costs to the government where they were material. A lack of a consistent approach can make some regulations appear to have much higher benefits or costs than others. A lack of comparability increases the difficulty of efficiently allocating resources to implement and enforce regulations.

17.39 These problems resulted partly from inadequate technical guidance from OPRA in the initial stages of implementation of the policy. In March 1989, OPRA issued a draft **Guide to Regulatory Impact Analysis**, which, in our opinion, represents state-of-the-art benefit and cost assessment. If this guide is followed by departments, a major improvement in the quality of analysis of proposed regulations can be expected.

17.40 Major improvements are needed in reporting information to the public on the impacts of regulations. We found that the departments we examined did not always report the required key information on proposed regulations in the RIAS. Unreported information has included important changes in regulations, significant commercial benefits to private sector firms, costs to the government and legislative authority issues.

17.41 Reporting of information on the use of alternatives to regulation is not required in the RIAS and in the annual Regulatory Plan. OPRA's process for developing regulations encourages departments to examine alternatives to proposed regulation that could achieve the same objective. However, departments are not required to report, either in the RIAS or the annual Regulatory Plan, the use of an alternative and its impacts. Interested parties may therefore be unaware of departmental action intended to achieve the same objectives as regulation.

17.42 Information in the annual Federal Regulatory Plan on departmental proposals to regulate can be improved. The annual Federal Regulatory Plan is a key means of making interested parties aware of proposed regulations. We found that some of the departments did not provide all the information required in the Plan, for example, the names of specific regulations to be revised, and basic information on anticipated impacts.

17.43 Furthermore, we noted that the information in the Plan does not allow interested parties to track the development of proposed regulations. The dates given in the Plan for publication in the Canada Gazette are often not met. The Plan does not provide interested parties with information that enables them to know the status of a proposal and the length of time it has been in development. In addition, where a proposal is not repeated in subsequent annual Plans, the reader cannot tell whether the proposal has been completed or dropped, or whether an alternative to regulation has been chosen.

17.44 Improvements are needed in the evaluation of regulatory programs in the departmental branches we audited. All four departments had plans for evaluating the regulatory programs we reviewed. Only one department had conducted and finalized program evaluations of regulatory programs. One of its two evaluations was satisfactory. Although another department had an evaluation planned for 1991, we found no evidence that the needed data had been developed. The 1982 evaluation of the same program also was hampered by the same lack of data.

17.45 Enabling legislation may lack provisions that allow departments to consider a range of regulatory options. Consideration of a full range of practical regulatory options may be constrained by an absence of legislative authority for a number of these options. For example, one department reported in its RIAS that a particular regulation limited production of ozone depleting chemicals to essentially two producers. The RIAS also indicated that this limitation may lead to price increases resulting in the transfer of hundreds of millions of dollars from about one thousand users to essentially the two producers of the product. The department could not obtain any benefits to taxpayers from the transfer of money resulting from its regulation through such measures as charging fees or auctioning off production rights. It stated that it did not have the statutory authority to undertake such options.

17.46 In our opinion, the scrutiny of regulations by the Standing Joint Committee is essential to maintaining parliamentary control over the regulating powers delegated to the government by Parliament. The work of the SJC focuses primarily on whether or not there is legislative authority for a regulation. For example, one of the Committee's major concerns is whether regulations provide discretionary authority to ministers and others outside of the powers specified in the legislation We found instances where the legislative authority for a regulation continues to be debated or a satisfactory solution was not implemented after many years of exchanges between the SJC and departments.

Recommendations

17.47 Departments should comply fully with OPRA's procedures for developing regulations. In particular, complete information on the impacts of regulations and any material rule changes should be reported.

17.48 OPRA's procedures should be extended to require departments to report the use and expected impacts of alternatives to regulation.

17.49 The annual Federal Regulatory Plan should contain information allowing interested parties to track the status of proposed regulations from year to year.

17.50 OPRA should strengthen its challenge and review procedures by selectively conducting in-depth reviews of information departments are required to provide in the RIAS and in the annual Regulatory Plan, to ensure that it is complete, reliable and comparable in the assessment of benefits and costs.

17.51 Departments should improve identification of the range of likely regulatory options for which they may need statutory authority so that legislation can be revised to remove constraints to desirable regulatory actions.

17.52 The Standing Joint Committee should consider extending its review to elements of the regulatory impact assessment statements. For example, it could review on a selective basis, the completeness of information in the RIAS relating to consultation and impacts. The SJC should also consider presenting periodic reports to Parliament summarizing the major issues of government-wide regulatory authority it has raised and the extent to which major concerns remain unresolved between particular departments and the Committee.

The Four Branches

Environmental Protection Directorate, Conservation and Protection, Environment Canada

17.53 The Environmental Protection Directorate (EP) of Conservation & Protection, Environment Canada, has primary responsibility for federal government efforts to control toxic chemicals and pollution, including the administration of the Canadian Environmental Protection Act and Section 33 of the Fisheries Act.

17.54 EP operates in complex circumstances involving the reconciliation of environmental protection requirements, industrial interests, socio-economic impacts, public pressures and federal-provincial jurisdictions.

17.55 We found strong support within Conservation & Protection for increasing openness, consultation and technical proficiency.

17.56 **Accountability**. In our view, Environmental Protection's procedures for setting priorities are satisfactory. A Priority Substances Panel, composed of scientists and representatives of industry, labour and environmental groups, recently proposed the Priority Substances List which was approved by the responsible Minister. This list of toxic substances will guide the Department's regulatory agenda for the next five years.

17.57 Although senior officials' accountability for regulations is clear, EP policies identifying roles and responsibilities at the working level for various aspects of the regulatory process have not been clarified.

17.58 Disclosure of plans to regulate. EP's activities are not always reflected in the Regulatory Plan. For example, EP has consulted extensively with certain interested groups in the last two years to revise the pulp and paper effluent regulations. The intention to regulate in this area was reported in the 1987 plan, but was not included in the plans for 1988 and 1989.

17.59 Consultation. In our opinion, EP has developed a model process for establishing a consensus on environmental protection measures among a diversity of groups. One objective of the process is to bring together all concerned parties or "stakeholders", to promote a common understanding of the issues. It is clearly described in the Environment Canada publication "From Cradle to Grave: A Management Approach to Chemicals". The process was successfully used to develop the Canadian Environmental Protection Act (CEPA) and the proposed amendments to the Environmental Contaminants Act.

17.60 However, EP has not extended this process to developing specific regulations that implement CEPA. Consultation on regulations is not guided by policies on how consultation should be structured, the type of information to be disseminated, the range of groups to be consulted and the records of consultation to be kept.

17.61 As a consequence we found evidence of inconsistent and unequal opportunities for consultation on regulations in EP as well as inadequate disclosure of information. We noted that EP tended to actively solicit the views of industry or technical advisers earlier than those of other groups, if not exclusively.

- During the last two years, industry and the provinces were consulted extensively on possible revisions to the pulp and paper effluent regulations. This consultation occurred prior to publication of the notice of intent to regulate in Part I of the Canada Gazette on 1 April 1989. Environmental groups had not had any significant involvement prior to this notice. EP explained to us that consultation with environmental groups and other interested parties has been initiated and that a discussion paper describing the proposed amendments will soon be made public.

- Results of a departmental study, indicating lack of compliance by the pulp and paper industry with effluent control regulations, were not made available to all concerned parties.

- On 21 June 1986 it was announced in the Canada Gazette that EP intended that leaded gasoline would be eliminated by 1992. Environmental, health and industry groups had the opportunity to make known their views about the 1992 cut-off date. After the announcement, environmental and health groups did not have a full opportunity to consult on the specific nature of the regulation. Industry, however, was consulted on such issues as how the regulation would be applied and enforced, the need for lead in specialized uses and when and where lead content would be measured.

- In contrast to the leaded gasoline regulations, public consultation on Phase One of the regulations to control chemicals that endanger atmospheric ozone levels was extensive with regard to certain control options.

- The proposal to amend the vinyl chloride regulations was announced in 1988. The revisions deal with measures to contain and report on releases of vinyl chloride into the atmosphere. EP documentation indicates that during the summer of 1988 their staff carried out a complete consultation with industry and the provinces involved concerning such issues as malfunction and emission trends reporting and accident prevention and preparedness. Our audit found that consultation with public interest groups had not taken place and that the final proposed amendments had been prepared by departmental officials. EP explained to us that the consultation process has not yet been completed and that it intends to carry out consultations with public interest groups prior to publishing the regulation in Part 1 of the Canada Gazette.

- Revisions to the Asbestos Mining and Secondary Lead Smelter regulations were not indicated in the RIAS approved by OPRA in July 1988 nor in 1989 when the RIAS for Asbestos Mining Regulations was published. The revisions included removing the requirement for an inspector to be present at **all** pollution tests ordered by the Minister, and adding a provision to allow the department to change the method of testing pollution emissions without changing the regulation.

Departmental response: *Regarding our observation on inconsistent and unequal opportunities for consultation, EP states:*

> *It is recognized that there is room for improvement in consulting with non-governmental organizations. It is nevertheless of utmost importance to consult industry promptly and in-depth on scientific and technical aspects to ensure that feasible and effective regulations are created.*

17.62 Cost and Benefit Assessment. Environmental Protection satisfactorily identifies regulatory options. Also generally satisfactory were its cost-benefit analysis of proposed ozone regulations, the information provided to Cabinet and Parliament on Ocean Dumping regulations, the information describing the compliance monitoring procedures for ozone depleting chemicals, and EP's guide on socio-economic analysis of pollution control.

17.63 At the same time, we found certain deficiencies. For example:

- Proposed ozone protection regulations would effectively restrict production of certain ozone depleting chemicals to essentially two Canadian producers. EP's studies, not widely circulated during public consultation, indicate that implementing the regulations may result in the transfer of $237 million to $348 million from 1,000 users of the chemical to essentially two producers. Alternatives which would obtain direct benefits for Canadian taxpayers, such as charging fees, or auctioning off production rights or combining quotas with the right of transfer, were identified, but in our view not adequately considered. EP explained to us that they do not believe they have the legislative authority to implement these alternatives because they were not provided for in the enabling legislation. EP indicated that given the Department's increasing public profile, senior officials are seeking solutions to the problem of limited authority in discussions with central agencies.

- Proposed gasoline regulations will phase out the general use of lead in gasoline by December 1990, rather than in 1992 as originally planned. The regulations will permit the use of leaded gasoline for critical and specialized uses in agriculture, marine activities and transportation. The rationale for an accelerated phasing-out of leaded gasoline is the harm lead causes to health. We did not find an assessment in the RIAS of the health consequences of continuing to permit certain uses.

- The impact of revisions to regulations controlling pollution from secondary lead smelters and asbestos mines was not assessed in the accompanying RIAS's.

17.64 Evaluation. The intent to evaluate specific regulatory programs was disclosed in the 1988 and 1989 Regulatory Plan. In March 1989, a revised draft five year program evaluation plan was prepared which includes CEPA programs.

17.65 Environment Canada has already completed two evaluation studies of three Environmental Protection programs.

17.66 We found that the evaluation of the industrial effluent and commercial toxic chemical control programs was not satisfactory. For example, data were inadequate on compliance with existing regulations. The evaluation of the Ocean Dumping Regulatory Program was satisfactory. The evaluation's scope and findings addressed key issues of effectiveness. For example, it found that "very little monitoring of Canadian disposal sites has been done and, as a consequence, there is no way of knowing whether or not an adverse impact has occurred".

Canadian Coast Guard, Transport Canada

17.67 The Marine Regulatory process is part of the Canadian Coast Guard activity in Transport Canada. Its overall objectives include developing and implementing regulations that contribute to marine safety and environmental protection.

17.68 Accountability. The Canadian Coast Guard has established a Legislative Affairs Review Council that includes key officials and is responsible for setting priorities and reviewing regulatory activity. Branch heads are regularly informed of the status of regulations.

17.69 Reporting of Plans to Regulate. In one third of the sample of regulations we examined, the information in the RIAS on the anticipated impact of the proposed regulations of Canadian Coast Guard was incomplete. For example,as explained below, information provided on the proposed Arctic shipping pollution regulations did not report anticipated commercial benefits to oil companies from extending the shipping season.

17.70 Consultation. The Canadian Coast Guard has established the Canadian Marine Advisory Council as the principal instrument of consultation. Representatives from industry and labour attend Council meetings. Provinces, municipal governments, industry and other interests are involved from the start of the regulatory process.

17.71 Cost and Benefits Assessment. We reviewed eight Canadian Coast Guard regulations. Cost benefit analyses had been conducted in five of the six instances requiring them. The methodology used in the cost benefit analyses could be improved. The information provided was incomplete in certain key areas. For example:

- Proposed pollution prevention regulations are designed to increase protection of the marine environment from oil discharges by ships and to allow Canada to accede to the Marine Pollution Convention. The RIAS submitted to RAB does not report that an uncertainty exists as to whether there may be additional reception facilities needed for ships to discharge bilge and, if they are required, whether the government or the private sector would pay for them. The Department informs us that a study is underway to determine whether or not additional facilities are required.

Arctic shipping pollution prevention regulations: an example of incomplete reporting of information

17.72 The 1988 Regulatory Plan included proposed amendments to extend the marine navigation season in certain Arctic Zones. On 1 February, 1988 DOT requested that Cabinet exempt the proposed regulations from normal prepublication in Part I of the Canada Gazette, on the grounds that it was an urgent, minor and routine amendment affecting only a small number of commercial vessels. The exemption was granted and the amendments were approved by Cabinet on 12 May 1988.

17.73 When the RIAS was drafted, a legal debate was in progress over the interpretation of the powers already granted to the Pollution Prevention Officers under section 15(3)(c) of the Arctic Waters Pollution Prevention Act, which could have made the amendment unnecessary. The RIAS did not report this fact. Our review also indicates that the information provided for Ministers on the regulations did not report the costs to the government and commercial benefits to the private sector. Further, no public consultation took place on these regulatory amendments.

17.74 On 2 September 1987 Oil Company A requested an extension of the navigation season to allow a certain type of ship in an area of the Arctic during a time period when the area is normally closed to such ships because of ice and other weather conditions. Although this extension was requested by the company to support its drilling program, the reason provided to the public for this extension was that "failure to implement these measures could result in increased damage to the environment in the event of an environmental emergency". The commercial benefits to Company A were not reported in the RIAS.

17.75 On November 4, 1987 Oil Company B requested an amendment to permit the M.V. Arctic, an experimental ship, to navigate in another Arctic Zone during a restricted season in 1988. The Company requested this extension to increase the amount of crude oil that it could remove. We found that the Department did not report the commercial benefits that would accrue to Company B resulting from this regulatory action. The regulation requires that a Coast Guard icebreaker be available to assist the ship before the ship can proceed. The cost to the taxpayer of such assistance also was not reported.

17.76 Evaluation. Transport Canada plans to complete its evaluation of the Marine Environment Protection and Clean-up Function, including related marine regulations in July 1989. The intent to evaluate was publicly reported.

Department's response: *Noting the effective date of September, 1986, for the new Federal Regulatory Action Plan, with respect to the drafting of Regulatory Impact Analysis Statements (RIAS) documents, the Department's regulatory initiatives that were the subject of the Auditor General's compliance audit were prepared in a complex transitional environment and finalized under the new guidelines.*

The Department is committed to the principles of openness, fairness, efficiency and accountability in the federal regulatory process and will comply with the intent of the new regulatory policy.

Bureau of Radiation and Medical Devices, Health and Welfare Canada

17.77 The Bureau of Radiation and Medical Devices (BRMD) is part of the Environmental Health Directorate (EHD), Health Protection Branch, Health and Welfare Canada. The Bureau's responsibilities include the developing of standards and regulations to reduce health hazards associated with medical devices and radiation sources. In 1989-90 the Bureau plans to improve the speed and efficiency of standards development by making direct reference in regulations to national and international consensus standards.

17.78 Accountability. A bi-weekly report on the latest status of proposed regulations is prepared by EHD. The report does not compare the current status with planned targets or explain problems being encountered such as delays.

17.79 The development of major policies governing the use of concensus standards as an alternative to regulation is unco-ordinated.

17.80 Disclosure of plans to regulate. The Environmental Health Directorate is significantly behind schedule in completing its regulatory actions. Excluding minor housekeeping amendments, we found that for 1989, EHD planned 24 regulatory actions, including 8 from the 1987 Plan and 9 from the 1988 Plan. The three regulations we reviewed had a 10 to 11 year development period. We found that interested parties had not been informed about the status of proposed regulations. Moreover, we are concerned that delays in the development of regulated safe performance standards may constitute a risk to the safety and health of medical device users. HPB indicates that "a delay in the establishment of a standard does not necessarily mean that enforcement action cannot be taken. The Food and Drugs Act itself can usually be applied if there is a risk to the health of the user".

17.81 Consultation. The Bureau of Radiation and Medical Devices has established an Advisory Committee on Medical Devices composed of representatives of various medical specialties. The Minutes of the Committee and its Sub-Committee on Medical Device Guidelines and Standards are sometimes inadequate on key issues. For example, they did not include the Sub-Committee's conclusions on draft criteria for voluntary standards to be adopted as regulations.

17.82 Disclosure of information on alternatives to regulation. As a result of regulatory reform, EHD may issue guidelines in lieu of formal regulations. EHD indicates that the decision to use a guideline as an alternative to regulation would be disclosed in the Annual Regulatory Plan as has been its past practice. The guidelines would be distributed to industry and interested parties by Information Letter.

17.83 Departments are only required to disclose formal regulatory proposals in the annual Federal Regulatory Plan. In our opinion, EHD's practice is more consistent with the principles of the regulatory process.

17.84 Evaluation. An evaluation of the Medical Devices program in the Environmental Health Directorate was to be completed in March 1990, but because of other priorities has been deferred to 1991. The last evaluation of the Medical Devices program, in 1982, encountered a lack of adequate data on device related hazards and injuries. We did not find evidence that the needed data had been developed for the upcoming evaluation.

Occupational Safety and Health, Labour Canada

17.85 The Occupational Safety and Health Branch (OSH) of Labour Canada is responsible for the administration of occupational safety and health programs. Its main work is the implementation of the provision of the Canada Labour Code which applies to companies under federal jurisdiction, for example, grain, banking and broadcasting. Approximately 34,000 entities with about 900,000 employees are covered, including all federal public servants.

17.86 Accountability. OSH has a clear definition of roles and responsibilities for the regulatory process. A detailed description of the process matches roles and responsibilities of officials against each stage of the regulatory process.

17.87 Disclosure of plans to regulate. The 1988 and 1989 Regulatory Plans refer to proposed revisions to a set of regulations. The specific regulations to be revised are not mentioned in either year. However, priority regulations for revisions were identified within OSH in 1986.

17.88 Consultation. OSH has implemented a satisfactory system for consultation on regulations and for setting priorities. At the centre of the system is a Review Committee chaired by Labour Canada and composed of labour and industry representatives. We found that both industry and labour are given ample opportunity to express their views in position papers and regular meetings.

17.89 Cost and benefit assessment. OSH conducts a cost and benefit assessment only of the regulatory option recommended by the representatives of labour and industry on the Review Committee, after lengthy negotiations. OSH states that it believes this procedure complements its compliance policy and is consistent with the government's regulatory review process. In our opinion, assessing only the chosen option reduces the usefulness of the analyses to the Review Committee, since other options cannot be compared to the chosen option.

17.90 In the two studies reviewed we found that there was room for a greater degree of technical rigour. OSH indicated that the level of analysis was limited by time pressures, data availability, resources and varying direction on methodology from central agencies.

17.91 We also noted that in its benefit and cost assessments of its regulations OSH does not estimate the monetary benefits of saving lives. OSH explained to us that it believes that its practice is consistent with OPRA procedures.

17.92 Evaluation. Labour Canada has an approved evaluation plan. The evaluation of OSH programs is in the beginning stages. The intention to conduct program evaluations has not been published in the Federal Regulatory Plan as required.

The Standing Joint Committee of the Senate and of the House of Commons for the Scrutiny of Regulations (SJC)

17.93 The Joint Committee for the Scrutiny of Regulations is a Committee of Parliament composed of members of the House of Commons and the Senate. Its role is to scrutinize regulations made by the Executive to ensure that they are authorized by legislation and conform to the requirements of the Statutory Instruments Act.

17.94 The SJC's scrutiny criteria include, for example, whether a regulation:

- is not authorized by the terms of the enabling legislation or has not complied with any condition set forth in the legislation;
- is not in conformity with the Canadian Charter of Rights and Freedoms or the Canadian Bill of Rights;
- imposes a fine, imprisonment or other penalty without express authority having been provided for in the enabling legislation;
- makes the rights and liberties of the person unduly dependent on administrative discretion or is not consistent with the rules of natural justice; and
- amounts to an exercise of substantive legislative power properly the subject of direct parliamentary enactment.

17.95 If the SJC believes there is an absence of legislative authority for a regulation, it normally writes to the department responsible for the regulation asking for corrective action. The department may agree or disagree with the Committee's views. We found that in certain instances exchanges between the Committee and a department have continued for many years.

17.96 During our special audit of the regulatory process we noted the matters raised by the SJC with the branches of the audited departments. SJC frequently raises important questions about the absence of legislative authority for departmental regulations. Some of the more important examples are described below.

17.97 The SJC informed Environmental Protection on 16 December 1977 and 17 March 1978 that its effluent regulations, under Section 33 of the Fisheries Act delegating ad hoc discretion to the Minister, are outside the Department's legislative authority. The matter remains unresolved after many years of exchanges between the Department and SJC.

The work of the Standing Joint Committee for the Scrutiny of Regulations is essential for maintaining Parliamentary control over regulation-making powers delegated to the government by Parliament.

17.98 The SJC informed Transport Canada on 11 June 1984 that it was of the opinion that Transport Canada did not have the authority to allow dangerous goods to be packed, marked, stowed or carried according to standards "equivalent" to those specified in the regulations. The Committee believed that such substitution must be specifically authorized in the enabling legislation. Concerns about this matter had initially been raised by the SJC in early 1982. In 1987 the Committee continued to note that while the Department cited various enabling authorities for the equivalency provision, the Committee did not agree that the cited authorities were appropriate. The Department believes that amendments to the 1987 Canada Shipping Act provide the authority. In November 1988, the SJC and the Department resolved the matter.

17.99 The SJC informed Health and Welfare Canada on 10 February 1975 that the Department's 1972 regulations had improperly delegated power to the Minister under a certain section of the Narcotic Control Act, managed by the Drugs Directorate, Health Protection Branch. Extensive correspondence ensued between the Committee and the Department. On 14 June 1988, the Minister informed the Committee that he intended to introduce legislation to rectify this and other issues. The legislation had not been introduced at time of writing.

17.100 In March 1985, the SJC wrote to Labour Canada regarding the Coal Mine Safety Regulations affecting the Cape Breton Coal Mines. SJC indicated that the Coal Mines Safety Officer's discretionary powers to vary or exempt the application of a regulation, or to approve mining methods, equipment or procedures, were not consistent with the Canada Labour Code. The powers were used to ensure that the standards applying to coal mining operations were appropriate to the changing mining environment.

17.101 Labour Canada sought amendments to the Code to provide clearer authority. These came into force in March 1986. According to Labour Canada the amendments caused serious problems for all parties concerned. After consultation, Labour Canada decided in February 1987 to again amend the Code, to establish a Commission with the authority to vary the application of regulations. Labour Canada assigned a high priority to these amendments. In 1988 the Code was further amended to enlarge the regulation making powers of Cabinet. The amendments also retroactively clarified the authority for the Coal Mines Regulations. As a result of the 1988 amendments, Labour Canada is revising its existing regulations. However, due to other government priorities, processing of the regulations was delayed. As of writing this process is not yet completed.

Office of Privatization and Regulatory Affairs
Bureau de privatisation et affaires réglementaires

Ottawa, Canada
K1A 1J2

July 26, 1989

Mr. Kenneth M. Dye
Auditor General of Canada
240 Sparks Street
Ottawa, Ontario
K1A 0G6

Dear Mr. Dye:

The Office of Privatization and Regulatory Affairs appreciates the special audit of the new federal regulatory process carried out by the Auditor General's Office. This review is timely and a welcome recognition of the importance to good government of efficient and effective regulatory management.

As an innovative and ground-breaking initiative for which there were no precedents anywhere in the world, it is perhaps not surprising that there have been some shortcomings and individual lapses during the early start-up phase of the program. Identification of the overall positive results of the program is gratifying and steps will be taken to address the difficulties brought out by your auditors.

Thank you for the opportunity to review and comment on the parts of the draft audit report which affect this department.

Yours sincerely,

Janet R. Smith

18

DEPARTMENT OF NATIONAL REVENUE - CUSTOMS AND EXCISE

Excise

18

DEPARTMENT OF NATIONAL REVENUE - CUSTOMS AND EXCISE

Excise

Main Points

18.1 Federal sales and excise taxes, totalling $17.2 billion in 1987-88, are a significant source of government revenue. Since 1985-86, annual revenue from the federal sales tax has surpassed revenue from corporate income tax. It was equal to about 30 percent of revenue from personal income tax in 1987-88 (paragraphs 18.7 to 18.9).

18.2 In the April 1989 federal budget, the government announced the introduction of the goods and services tax to replace the federal sales tax in January 1991 (18.13 to 18.19).

18.3 The population of taxpayers is expected to increase by at least 13-fold, from 75,000 to over 1 million, and the mechanics of the new tax will be completely different. The Department faces an unprecedented challenge in preparing to implement it. It will need to give it the priority and resources required to ensure the successful delivery of this major government initiative (18.25 to 18.50).

18.4 We found certain weaknesses in the Excise Branch's administration of the federal sales tax, including:

- the level and scope of enforcement activities have been decreasing over time;
- information on performance and compliance has not been adequate, and data have not been used to the best advantage for program administration;
- certain departmental practices have gone beyond legislation; and
- tools and staff training could be improved.

It is important for the Department to analyze and correct the causes of these weaknesses, and not to run the risk of repeating them under the new tax regime (18.23 and 18.24).

18.5 The federal sales tax will continue to be an essential revenue program until it is replaced. During the transitional period, while the Excise Branch plans for the new tax, it must also be vigilant in safeguarding revenue and maintaining the integrity of the system to minimize revenue loss (18.132 to 18.137).

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DEPARTMENT OF NATIONAL REVENUE - CUSTOMS AND EXCISE

Excise

Background

18.6 The Excise Branch of the Department of National Revenue - Customs and Excise administers the Excise Tax Act and the Excise Act and their regulations. The Excise Tax Act and regulations impose federal sales tax (FST) on manufactured goods and excise taxes on goods such as cosmetics, jewelry, wine and gasoline. The same legislation also imposes a tax on certain insurance premiums, the air transportation tax, the telecommunication services tax and the telecommunication programming services tax. The Excise Act and regulations impose excise duty on liquor, beer and tobacco products.

Federal sales and excise taxes contribute significantly to the total revenue which finances government program delivery.

18.7 The federal sales and excise taxes contribute significantly to the total revenue which finances government program delivery. Over a five-year period, this revenue has grown from $7.8 billion to $17.2 billion for 1987-88. The federal sales tax forms a major component of this revenue.

Federal sales tax -- its nature and significance

18.8 The FST is a tax imposed on manufacturers and those who are deemed to be manufacturers under the Excise Tax Act. The tax applies to the manufacturer's sale price for goods produced in Canada and to the customs duty paid value of imported goods.

18.9 In 1987-88, the sales and excise taxes of $17.2 billion represented 17.7 percent of total federal government revenue. The FST component alone was well in excess of the corporate income tax revenue of $10.9 billion and was equal to about 30 percent of the revenue from personal income tax (Exhibit 18.1). Exhibit 18.2 shows the growth of the revenue from FST since 1983-84. It surpassed that from corporate income tax in 1985-86. The general rate of sales tax was set at 12 percent in 1986. In the April 1989 federal budget, the Minister of Finance announced a sales tax rate increase to 13.5 percent, effective 1 June 1989 and forecast an annual revenue increase of $1.6 billion. Many manufacturers will continue to pay more federal sales tax than income tax.

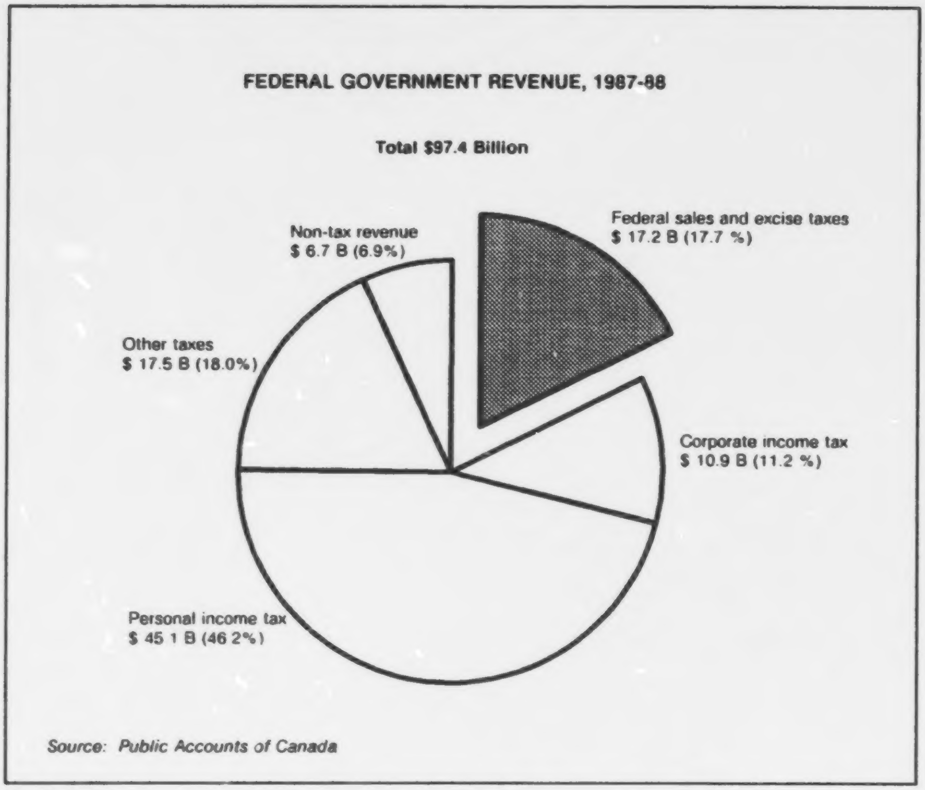
Organization of the Excise Branch

18.10 The Excise Branch of the Department is responsible for the administration of the sales and excise taxes and duties. The Department of Finance is responsible for tax policy and legislation.

18.11 The Branch identified six sub-activities in its Part III of the Estimates document:

- tax interpretations;
- verification and enforcement;
- revenue accounting and collections;
- appeals;

Federal sales and excise taxes contribute significantly to total government revenue.



FEDERAL GOVERNMENT REVENUE, 1987-88

Total $97.4 Billion

Source: Public Accounts of Canada

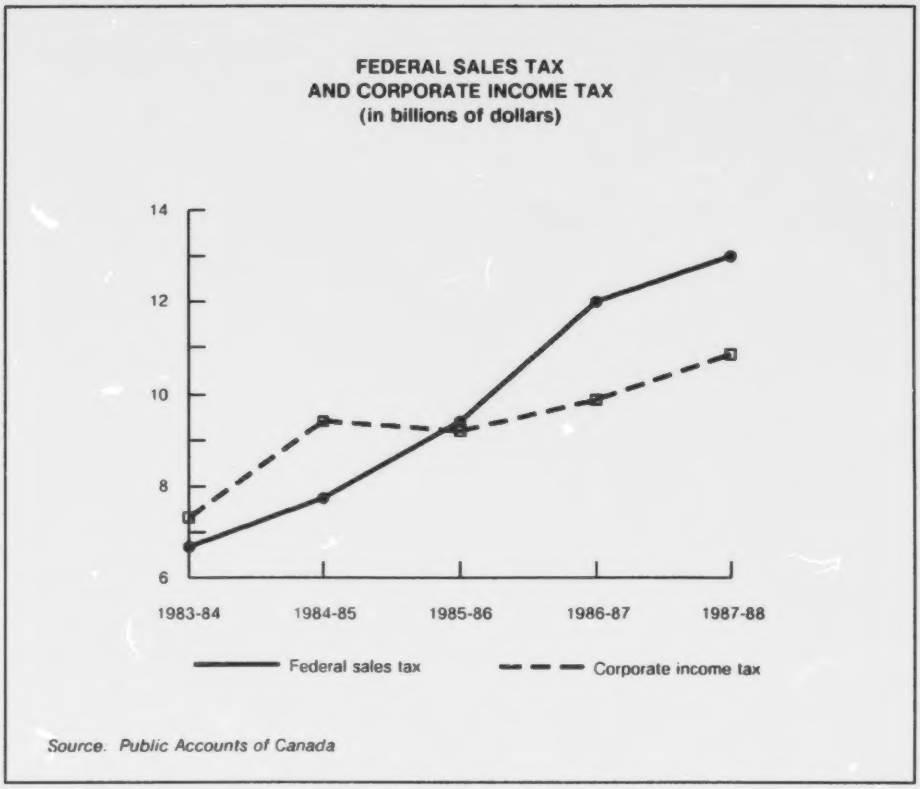
Exhibit 18.1

- policy and systems; and,
- program management and support.

The tax interpretations sub-activity provides rulings and other information to taxpayers. It also identifies and licenses them. The verification and enforcement sub-activity involves verifying and processing refund claims, auditing taxpayers and conducting special investigations and duty surveillance. Revenue accounting and collections deals with depositing and accounting for revenue. In addition, it takes collection actions against delinquent taxpayers. The appeals sub-activity provides an independent system that addresses objections raised by taxpayers. The remaining two sub-activities provide linkage to the Department of Finance and overall support to the Branch. In 1987-88, the Branch had a staff strength of about 1,600 person-years and expenditures of $82 million. The resource allocation among the sub-activities is depicted in Exhibit 18.3.

18.12 The Branch's administration is decentralized. The functional groups at head office deal with programs, administrative policies and procedures. They provide functional direction and monitor operations in the regions. The regional offices, district and sub-district offices deal directly with the public in a range of activities including licensing, interpretation, audit, refund, tax collection and revenue accounting. The regional directors report directly to the Branch Assistant Deputy Minister. There are 9 regional offices and 27 district and sub-district offices.

Federal sales tax revenue has surpassed that of corporate income tax since 1985-86.



Source. Public Accounts of Canada

Exhibit 18.2

Budget announcement to replace federal sales tax

18.13 It has been widely accepted that the FST system is flawed. Since the Excise Tax Act came into force in 1924, there have been numerous studies pointing to its faults.

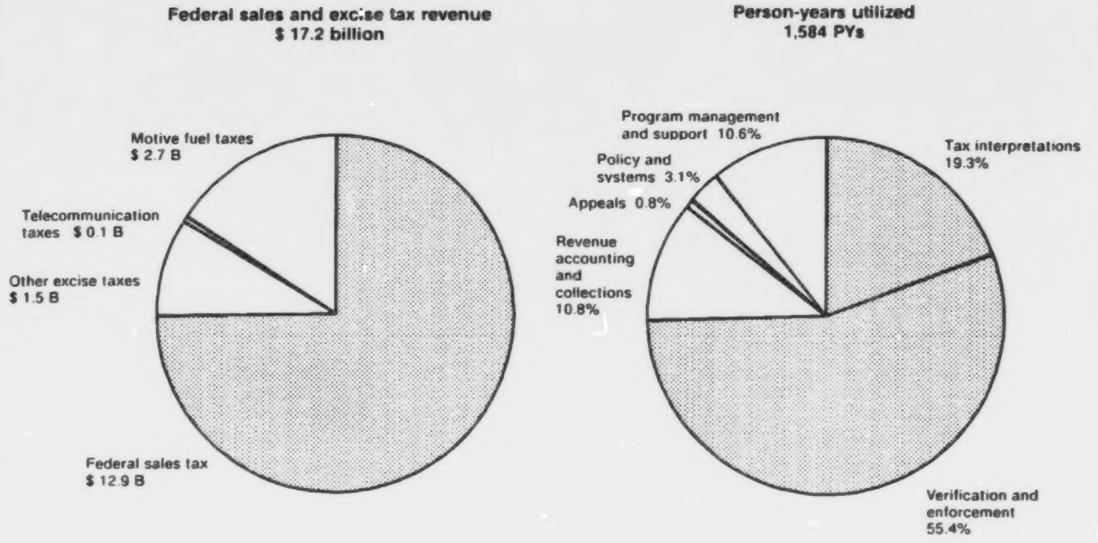
18.14 In the April 1989 budget documents, the government stated that the FST is limiting economic growth and job creation and that it is impeding the country's ability to compete internationally.

18.15 The archaic structure of FST, coupled with its numerous exemptions, special provisions and administrative practices that have developed over time, is rendering the existing sales tax system increasingly difficult to administer. It is also becoming more difficult to maintain proper safeguards against tax avoidance.

18.16 The June 1987 White Paper on Tax Reform proposed adopting a broad-based multi-stage sales tax system which would extend to the retail level. In the April 1989 federal budget, the Minister of Finance announced the introduction of the goods and services tax (GST) to replace the existing FST effective 1 January 1991.

18.17 According to the budget documents, the GST will be imposed at a nine-percent rate. It is a tax that will ultimately be borne by the final consumer. All businesses throughout the production and distribution chain will charge tax on their domestic sales but will be able to claim a credit for all GST paid on their inputs.

EXCISE BRANCH, 1987-88



Sources: *Public Accounts of Canada*
Part III of Estimates

Exhibit 18.3

18.18 Unlike the FST, the new tax will apply to most goods and services consumed in Canada. The budget documents indicated that there will be relatively few exceptions. The exceptions announced to date include certain goods such as basic groceries, certain services such as residential rents, as well as special arrangements for certain suppliers such as hospitals, municipalities and registered charities.

18.19 The government planned to release a detailed technical paper on GST in early summer 1989. Following this release, hearings would be held on the proposal. The government also intended to release draft legislation in the summer of 1989 and expected to introduce final legislation in Parliament in the fall of 1989.

Audit Objective and Scope

Audit Objective

18.20 Our audit objective was to review and assess the Branch's operations in key areas of administering the FST system and to identify opportunities for improvement. With tax reform on the horizon, we were also looking at existing problems and weaknesses that could occur in the new sales tax system, with a view to highlighting them so that they can be analyzed and corrected.

Audit Scope

18.21 We examined the two major sub-activities, tax interpretations and verification and enforcement, because they involve about 75 percent of the Branch's resources. Our examination included the functions of licensing, interpretation and rulings, audit and refunds. We also examined performance measurement and human resource management within the Branch, focussing on the same two sub-activities. We reviewed the other sub-activities, such as appeals and policy and systems, only to the extent that they related to issues within the scope of our audit.

18.22 We conducted our audit at head office and visited seven of the nine regional offices. For human resource management issues, we also interviewed staff from the Personnel Administration Branch and the Customs and Excise College in Rigaud, Quebec. In addition, we held discussions with staff from the Corporate Management Branch on matters relating to performance measurement.

Sales Tax Reform -- Its Implications for Tax Administration

Problems and weaknesses in federal sales tax administration need to be analyzed and taken into consideration in planning the administration of the new tax

18.23 Our audit observations centred around the following four areas, which are discussed in the latter part of the chapter:

- The level and scope of enforcement activities have been decreasing over time (paragraphs 18.51 to 18.79)
- Performance and compliance information has not been put to the best use for program administration (paragraphs 18.80 to 18.94).
- Certain departmental practices are beyond the legislation (paragraphs 18.95 to 18.111).
- Tools and training present opportunities to improve the cost-effectiveness of the sub-activities' operations (paragraphs 18.112 to 18.131).

GST Implication

18.24 It is important for the Department to analyze these weaknesses and take measures in planning the GST implementation to minimize the risk of repeating them in the new tax regime.

Tax reform will bring a massive change to the administration

18.25 The new GST differs from the FST in two significant ways -- the greatly increased population of taxpayers and the new mechanics of the tax which will be applied up to, and including, the retail level.

18.26 With the new tax, the tax base will be extended to most goods and services. In addition, it will be charged by all businesses throughout the production and distribution chain. As a result, a massive increase in the number of registered taxpayers is anticipated under GST.

18.27 The FST taxpayers are required to be licensed under the Excise Tax Act. These registered taxpayers are known as licensees. Approximately 75,000 licensees are registered under the existing system. Since the new tax will have to be collected and paid by virtually all businesses, the increase in the number of registered taxpayers will be significant. The final number will depend on the exemption threshold for small traders. Nevertheless, the number of registered businesses is expected to exceed 1 million, representing at least a 13-fold increase in the taxpayer population.

18.28 The budget documents described the new tax as a multi-stage sales tax. The mechanics of the GST will involve all businesses in the production and distribution chain and require them to charge tax on their sales. However, the tax paid on purchases by a company will be offset as an input tax credit against the sales tax collected; the company will only have to remit the net tax. Should the tax credit exceed the sales tax in the reporting period, the company will be entitled to a refund.

18.29 The mechanics of the GST will introduce a new dimension to the sales tax system -- accounting for refundable invoiced-based input tax credits. The volume will be significant, as it applies to all trade levels.

The Department will face an unprecedented challenge in planning and implementing the goods and services tax administration

18.30 The GST is a federal-only, value-added tax. The government proposed it as one of three options in the June 1987 Sales Tax Reform paper. In this paper, the government favoured the option of having a joint federal-provincial national sales tax system because it could offer major gains in efficiency and simplicity to administrators and taxpayers. The April 1989 budget documents stated that after reform at the federal level is complete, the idea of an integrated national tax can be explored once again. However, in the meantime, the Department will have sole responsibility for administering the new tax.

18.31 Under these circumstances, we noted the following aspects of this major challenge to the Department:

- staffing and training;
- information services to taxpayers;
- new population of taxpayers;
- information and system support;
- co-ordination with other organizations; and
- federal sales tax rebates.

18.32 **Staffing and training.** In order to administer and collect the tax and serve over one million taxpayers, the Department will have to significantly increase its resources. This could result in a two- to three-fold increase in staff strength in the Excise Branch.

18.33 Recruiting and staffing this many positions for a decentralized department like Customs and Excise will be a major undertaking. In addition to the difficulties involved in identifying suitable candidates, many of these positions will be required in the regions which could pose some further staffing problems. New and existing staff will have to be trained to deal with the GST; this will involve a large-scale training program.

18.34 **Information services to taxpayers.** A self-assessment system demands that taxpayers be made aware of which ones are liable for the tax, what taxes they owe, when the taxes are due, and how they ought to file information returns with the Department. The onus is on the Department to provide information support to taxpayers so that they can voluntarily comply.

18.35 This function becomes even more important with the introduction of a new tax regime. In addition to having to account for the tax paid on inputs to claim credits and refunds, businesses will have to learn to understand exceptions to the GST. Where the exemption status of the sale is different at the federal and provincial levels, retailers will have to contend with a dual system. Further, the multi-stage nature of GST will require payment of tax at the time of input purchases. In some cases, this will increase the burden on cashflow, and all businesses throughout the production and distribution chain will be anxious to know how to claim their tax credits in an expeditious and timely manner.

18.36 The Department will have to educate its own staff as well as the public well before the implementation date of GST.

18.37 **New population of taxpayers.** Tax reform will bring with it a massive increase in the size of the taxpayer population. The new population will extend far beyond manufacturing activities to the service sector, retailers and non-profit organizations.

18.38 The Department will need to gain knowledge of this new "clientele". In order to provide effective checks and balances in the new regime, it will have to identify areas with high risks and be vigilant to guard against revenue leakage and maintain the integrity of the new tax system.

18.39 **Information and system support.** The GST administration will require new information and system support. The Department will need to assess its performance measurement system, modify existing performance indicators, and identify and put in place new indicators to provide a compliance monitoring framework and to support management decisions on GST administration.

18.40 In addition to the high volume record-keeping requirements, the Department will have to build a database for the GST taxpayers. It will need to assess its data processing requirements and acquire further computer system capability. The Department was in the process of implementing a comprehensive computerized system for its FST administration. The phased implementation for that system will have to be re-examined as it begins its system development planning for the GST.

18.41 **Co-ordination with other organizations.** The majority of the population of taxpayers under GST will also be subject to federal corporate income tax. At the retail level, the same businesses will be subject to both GST and provincial retail sales tax.

18.42 This provides an opportunity for the Department to share the experience gained by the other government organizations that manage those tax programs. The Taxation Department has long been developing and maintaining large-scale computerized revenue and tax assessment systems. It also has the groups and systems in place for profiling high risk industries and conducting special investigations. The provinces, on the other hand, have long-standing machinery for interacting with retailers. These retailers, representing the last trade level collecting the GST, form a significant segment of the taxpayer population and are the most susceptible to revenue loss.

18.43 This situation creates a challenge as well as an opportunity. While the Department can benefit from consultation with these organizations, it will have to take a lead role and co-ordinate its activities with them to make administration as efficient as possible and to minimize the burden on taxpayers.

18.44 Federal sales tax rebates. On implementation of GST, many firms will be holding inventories for resale on which FST will have been paid. In the April 1989 federal budget, the government announced that it would provide rebates of FST on these inventories.

18.45 It will be a major task to estimate the FST portion of the inventories held; it is not only a hidden tax but the variation in effective rates of the tax on goods with the same statutory rate is astounding. A 1985 survey conducted on behalf of the Department of Finance showed that the ratio of the highest to the lowest effective FST rate for the same groups of commodities ranged from 1.3 to 3.3. For example, competing small appliances were taxed from a high of 12.4 percent to a low of 4.9 percent -- a spread of 7.5 percentage points, a highest-to-lowest ratio of 2.5. There will also be wide variations in taxpayers' ability to determine for themselves the FST component in their inventories. The Department will have to formulate guidelines to help them and provide a basis for verification and enforcement.

18.46 In principle, all businesses with inventories held for resale could come forward and claim a rebate. The Department is anticipating a significant volume of claims, which will be filed within a relatively short period of time. The Department will have to assemble the machinery to verify and process these claims.

18.47 This major task of converting tax-paid inventories to pre-tax levels will pose threats of revenue leakage. The Department will have to provide proper controls over the conversion process to ensure a fair assessment of the rebates and minimize revenue loss.

Sales tax reform -- making it work

18.48 The reform of the federal sales tax is regarded by the government as a key element of its strategy to safeguard essential programs and strengthen Canada's economy. It also presents an opportunity for Canada to move to a sales tax system comparable with that of many of the other industrialized countries.

18.49 The Department is facing an unprecedented challenge in this reform. We have concerns about the administration of the existing system which need to be considered in planning the delivery of the new tax. However, the implementation timetable will be extremely tight. As of April 1989, the Department had only 20 months to make the system operational. The bill introducing GST legislation in Parliament was not expected until the fall of 1989, which would be about 15 months before the effective date of the new tax. Within that time, the Department has to develop and carry out its implementation strategy. Furthermore, it has to provide information and guidelines to businesses, giving them sufficient lead time to modify and redesign their systems to calculate, account and report the GST by its effective date of 1 January 1991.

GST Implication

18.50 It is imperative that the Department give priority to meeting the challenge, so that the risk of a setback is minimized. A well co-ordinated start would reduce frustration and confusion and would go a long way toward ensuring the future success of this major revenue system. The Department will also require appropriate resources to deliver the new system.

Level and Scope of Enforcement Activities - Decreasing over Time

The changing environment has placed increasing pressure on the existing system

18.51 The federal sales tax was put in place in 1924. Over the years, it has not kept pace with the business environment. Further, with the broadening of the definition of manufacturer and the long list of exemptions, it is becoming increasingly difficult to administer.

18.52 The difficulty is compounded by the growth of the tax consulting industry surrounding the FST. Many consultants offer services, often for contingent fees, to manufacturers and their customers to seek out refunds. The number of refund claims climbed from about 90,000 to almost 140,000 in the five years from 1983-84 to 1987-88. The value of refunds paid over the same period more than doubled to $622 million (Exhibit 18.4).

18.53 In addition, more and more companies are coming to realize that FST is a significant cost of running a business and are becoming more sophisticated and aggressive in attempting to arrange their affairs to minimize their tax liabilities. This has led them to seek out areas where legislation is weak. It has resulted in actions such as shopping for rulings in different regions and the creation of marketing and distribution companies.

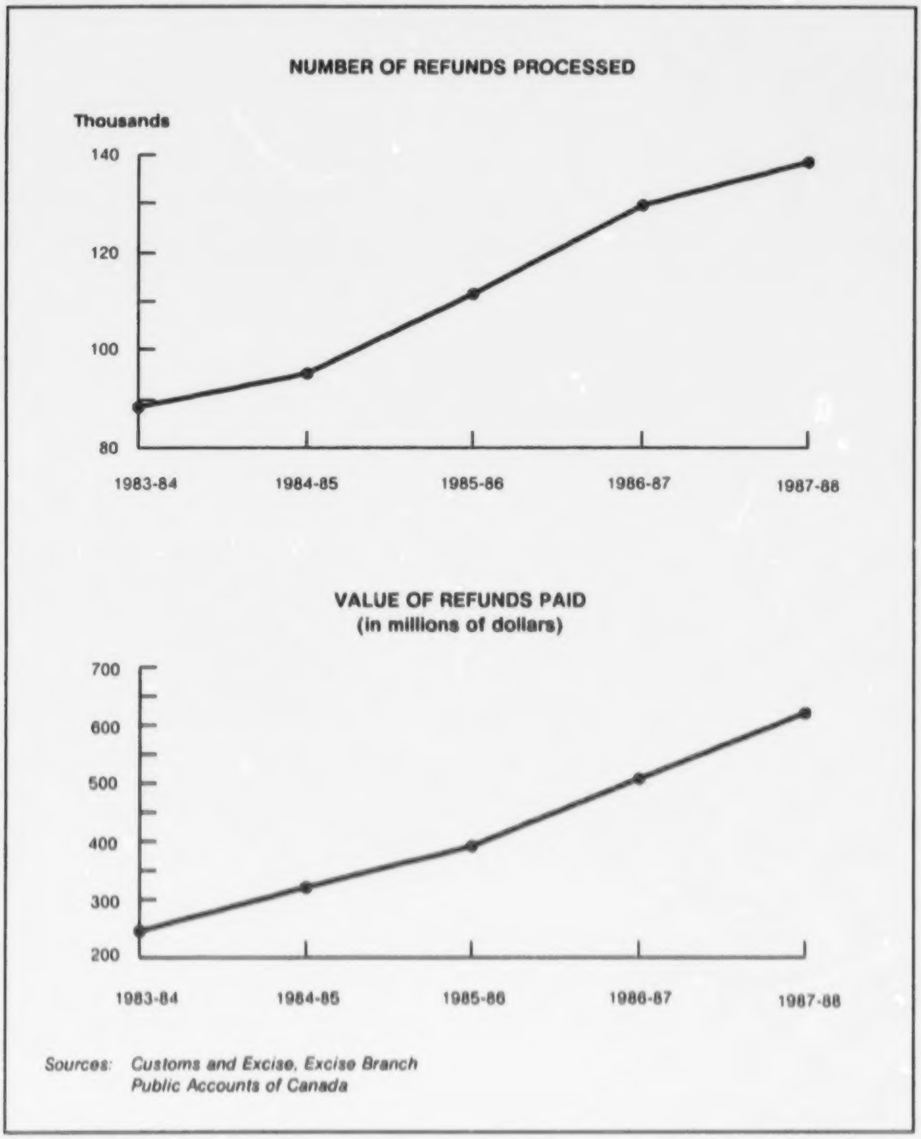
Enforcement levels and activities have been falling behind

18.54 In recent years, in an attempt to encourage voluntary compliance, the Excise Branch increased its emphasis on facilitation through taxpayer visitation and assistance projects. The use of facilitation person-years increased by 45 percent over five years, from 210 PYs in 1983-84 to 306 PYs in 1987-88. During this time, the number of person-years used for enforcement has remained relatively stable. However, in the meantime, the enforcement workload has increased. Over the last five years, the number of licensees increased by 27 percent from 58,000 to 74,000. Also, within the sub-activity, priority has been given to other activities, such as the processing of refund claims and special projects, which has further reduced the availability of enforcement resources for regular sales tax audit.

18.55 The emphasis on service to taxpayers is also shown in the key measures of effectiveness used for the audit function. Audit results are primarily measured using the concept of tax change. Under this concept, both debit and credit assessments are included for measuring audit effectiveness. For example, a $100 debit assessment coupled with a $100 credit assessment on a single audit would yield a $200 tax change measure, although it has no impact on net revenue. Although net revenue measures are also calculated, they are rarely included in management reports.

18.56 It is the mandate of the Department to assess and collect the proper amount of tax. To fulfil this mandate, auditors should grant credits when a taxpayer overpays his taxes. The question becomes where the responsibility of the auditor for identifying that overpayment ends and that of the taxpayer begins. In pointing out the potential exempt area to the taxpayer, the auditor could be considered to have discharged his responsibility. Due to the transaction-oriented nature of the FST, going on to determine the actual amount of the credit usually requires more audit work which would further reduce the availability of scarce enforcement resources. In addition, it is unfair to the taxpayers who compute their credits and bear their own compliance costs. The Branch advised us that in its call letter for 1989-90, auditors were asked, wherever practical, to encourage taxpayers to perform the work involved in establishing credits.

Refund claims have increased substantially over the last five years.


NUMBER OF REFUNDS PROCESSED

VALUE OF REFUNDS PAID
(in millions of dollars)

Sources: Customs and Excise, Excise Branch
Public Accounts of Canada

Exhibit 18.4

18.57 The Branch's assessment practice for new licensees is a further illustration of its emphasis on service to taxpayers. We noted that in conducting licensee investigations, the auditors would audit and assess back taxes only if they determined that the new licensee was aware of the licensing requirement. The Branch has viewed this practice as a means of providing the taxpayer with the benefit of the doubt of not understanding the licensing implications of the legislation. However, under the Excise Tax Act, the Branch has the authority and responsibility to assess and collect FST for the preceding four years. This assessment practice is not in keeping with the Department's mandate of assessing and collecting the proper amount of tax. It is also a quasi-amnesty program which has not been sanctioned by law and has not been made known to all potential licensees. If the

Department wishes to continue this practice, it should seek legislative support and publicize the policy.

18.58 The increase in the number of licensees, coupled with an increasing workload due to refund claims and a changing environment, has had some visible impact on enforcement activities:

- a marked decline in audit coverage; and

- an almost non-existent ongoing licensee identification activity.

It is the Department's objective to collect revenue and foster voluntary compliance. The audit function is very important in providing the proper checks and balances for a self-assessment system. A weakening audit function undermines the deterrent factor and compromises revenue generation.

18.59 **Marked decline in audit coverage.** The reduction of audit resources has resulted in a marked decline in audit coverage over the years. Departmental data have shown record low rates of audit penetration (Exhibit 18.5). The preliminary figures for 1988-89 indicate a continuing trend of decline, with a penetration rate of less than seven percent.

18.60 Moreover, the Excise Branch has maintained a similar approach to audit selection over the years in spite of increasing workload. Special projects and the audit of certain groups of licensees, such as large manufacturers, were categorized as mandatory audit workload. The selection of the "jumbo" audits has been adjusted over time. However, these and the special projects continued to erode the ability to conduct discretionary audits of the licensee base at large. To the extent that discretionary audits were done, the selection was made on the basis of risks identified through the computerized Responsible Audit Services Program (RASP) whose database was limited and not up to date. Updating the RASP database is dependent on audit results. The decline in audit coverage has further limited the reliability of RASP to profile the audit risk of licensees.

18.61 The Branch's audit philosophy has been based on revenue payback. The jumbo audits were given priority because they were considered to have the most revenue impact. The RASP selections were made with a view to auditing higher risk licensees. The emphasis on payback was made at the expense of encouraging voluntary compliance and providing a deterrent effect.

18.62 In October 1987, the Branch reported: "In a period characterized by sharply increasing tax rates and an increasing tax scope, reduced audit penetration could result in a steady erosion of the protection of revenue over an extended period of time." In her June 1988 Annual Management Report to the Treasury Board, the Deputy Minister expressed her concern:

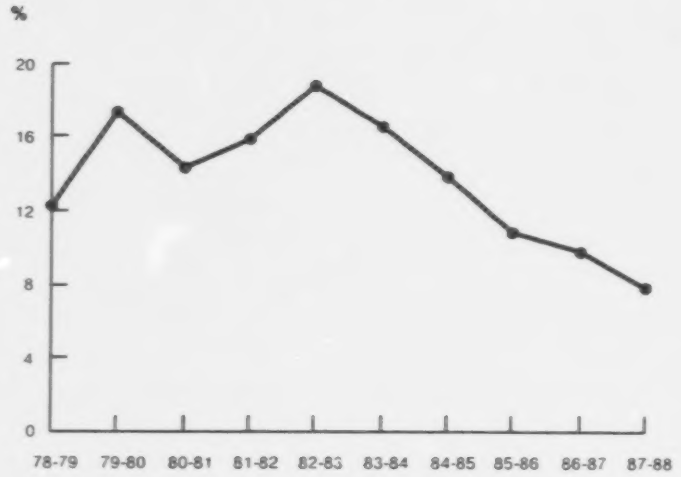
> With our reliance on voluntary compliance and deterrence through selective enforcement, we are reaching dangerous levels with respect to the risk of non-compliance.

18.63 Since 1987, the Branch has been developing an initiative to increase audit coverage. At the time of our audit, the Department was planning to implement a new audit program in 1989-90. Its stated objective is to increase the audit coverage, update its licensee database and confirm its risk categories.

18.64 However, the Branch has not been able to meet its planned audit coverage in recent years. With the existing resources, we are concerned that the extent of the planned coverage will not be achievable without a significant cutback in audit scope and examination. The Branch's objective of enhancing its audit presence among licensees will

There has been a marked decline in audit penetration rate over the years.

AUDIT PENETRATION RATE



Source: Customs and Excise, Excise Branch
Audits as a percentage of active licensee accounts.

Exhibit 18.5

not be properly served if these dimensions of the audits are excessively curtailed. The Branch will need to stress the quality and depth of audits to achieve the desired deterrent effect.

18.65 The statement of objectives also included a reference to updating the licensee database and confirming the RASP risk categories. Samples of licensees are to be drawn by the regions on the basis of the existing risk categories. This sampling plan will not be conducive to drawing statistical conclusions. Because of RASP's limitations, it also might not provide the best payback. The Branch could complement its RASP selection with industry-specific or issue-oriented enforcement work.

18.66 Although the Department is less than 20 months away from the implementation of GST, there are statutory provisions allowing for audit and verification up to four years after the date of assessment. During this time, the Department must be vigilant in keeping the system honest and protecting this major source of the government's budgetary revenue.

18.67 The Department should maintain a vigilant enforcement program to promote voluntary compliance and maximize payback. It should make every attempt to meet its new coverage objective, and complement its plan with other enforcement efforts.

Department's response: *The Department fully agrees that an enforcement program to promote voluntary compliance and maximize payback is essential. We have tried to maintain an appropriate balance between enforcement and facilitation, compatible with the* *departmental operating principle that most taxpayers are honest and willing to pay the correct tax when adequately informed. Every effort will be made to meet the new audit coverage objectives, consistent with available resources in the context of the elimination of FST. In this regard, working paper requirements have been modified to permit increased audit efficiency. In addition, specially targeted reviews in high risk industry sectors will continue to be undertaken.*

GST Implication

18.68 In administering a revenue system, the Department will always need to strike a balance between facilitation and enforcement. This balance requires evaluation from time to time and adjustment where appropriate. When resources are scarce, it becomes more important to review the approach being taken and to consider alternatives. These principles will continue to apply under sales tax reform.

18.69 Ongoing licensee identification activity was almost non-existent. Under the Excise Tax Act, all manufacturers and producers other than those exempted are required to apply for licenses. The licensing function is part of the tax interpretations sub-activity. It consists of a licensing service, which reviews the applications and issues the licenses, and licensee identification, which seeks out and identifies taxpayers who ought to be licensed. Licensees are periodically required to file returns and remit federal sales tax collected.

18.70 The licensee identification function is significant for a number of reasons. First and foremost, the Excise program objective is to assess and collect the proper amount of taxes due under the legislation. In support of this objective, the Branch has stated as a sub-objective that "eligible taxpayers are identified and licensed". It is an integral part of the Branch's mandate to identify and license taxpayers to maintain the integrity of the system.

18.71 Also, a weak licensee identification function can result in disparity and unfair competition in the affected industries, as well as loss of revenue. Unlicensed manufacturers and producers could avoid charging sales tax on the goods they sell and thereby gain a competitive edge over properly licensed taxpayers.

18.72 Moreover, an unlicensed manufacturer escapes the enforcement function of audit. The Branch's audit coverage and selection are limited to the existing licensee base.

18.73 Identification efforts were made at the time when budget initiatives and legislative changes were introduced. However, ongoing licensee identification was almost non-existent. In our regional visits, we found virtually no ongoing identification activity initiated by the Branch. Licensee investigation normally took place following requests by manufacturers and in response to complaints from competing manufacturers.

18.74 We found that, in 1985, head office had instructed the regions to terminate the licensee identification function beginning in 1986-87. Resources were redeployed to issue rulings to taxpayers. This demonstrates how initiatives and cuts were often at the expense of enforcement.

18.75 However we found that, in two of the smaller regions where the regional directors took the initiative of having their staff conduct some identification work, there have been encouraging results. For example, in Calgary, 212 potential licensees were identified and contacted. This resulted in 18 new licensees, an 8.5 percent success rate. When analyzed according to industries, the success rate ranged from 5.3 percent to 13.3 percent. The new licensees are now subject to filing and remittance requirements and fall within the enforcement net of audit. The regional experience showed that such enforcement actions are feasible and have good potential payback.

18.76 Licensee identification was reinstated for 1988-89. In the call letter for 1989-90, the head office instructed the regions that:

> A program of identification of potential licensees is to be maintained to ensure that all persons requiring a license are identified, investigated and licensed.

Although the regions have been instructed to resume the licensee identification function, they have not been given additional resources. The function is considered to be a regional responsibility and there is no national co-ordination.

18.77 While it may not be cost-effective to have a comprehensive identification program in the final days of the existing FST system, we believe that enforcement actions need to be resumed to protect the system and provide fairness to the taxpayers who comply with it.

18.78 The Department should strengthen its licensee identification function by providing more central support such as resourcing, co-ordination and monitoring to ensure the integrity of the sales tax system.

Department's response: *As mentioned in the Audit, the regions have been issued instructions on the identification of potential licensees, in the 1988-89 work plan call letter. However, we do not believe it would be cost-effective to divert decreasing FST resources to this function for increased central support. Licensee identification is to be recognized as a special attention area in GST program development.*

GST Implication

18.79 The implication of licensing will be different under the new tax. Nevertheless, some businesses would choose not to be registered. With an anticipated increase of over 13-fold in potential taxpayers under GST, it is critical that taxpayer identification become an integral part of the Department's enforcement activity.

Performance and Compliance Information -- Not Adequate and Not Put to the Best Use for Program Administration

18.80 The Excise Branch has established a detailed performance measurement and reporting system to gather information on the Branch's activities. The system has been in operation for a considerable period of time and was one of the contributing factors to the signing of the Memorandum of Understanding with the Treasury Board to participate in the Increased Ministerial Authority and Accountability (IMAA) initiative.

18.81 The system generates data for the monthly performance reports and the Branch Operations Quarterly Reports. These form the basis of the Departmental Performance Reports to senior management. Since 1988, the reports have also been sent to Treasury Board quarterly.

Performance and compliance information has not been adequate to support the Branch's management of the FST system

18.82 We found that there are abundant quantitative measures in the Branch. Every sub-activity has some measures of input, workload and output, and variances from targets based on historical data are reported regularly.

18.83 On the other hand, we found gaps in information on performance and limited analysis for managing Branch activities. In particular, the performance measurement system has fallen short of meeting one of the Branch's objectives -- to determine the degree of compliance. It has not been providing a framework for ongoing monitoring of taxpayers' compliance to support Branch planning and resource deployment. For example, the Branch has not been in a position to know:

- the extent of non-compliance in key industries and the estimated revenue loss;
- the potential effect of a declining audit penetration rate on taxpayers' compliance; and
- the level of service and the adequacy of the information provided to taxpayers by the tax interpretations sub-activity.

18.84 In 1987, a Branch document stated that "it is necessary to have a capacity not only to determine the degree of compliance, but to enforce compliance so as to act as a deterrent to non-compliance".

18.85 We noted that the Department's March 1989 draft Departmental Accountability Regime document included some effectiveness and level-of-service indicators. However, it does not address the need for a compliance monitoring framework or our concerns on weaknesses in other effectiveness measures.

18.86 We also found that there were limited resources for research and analysis within the Branch. Many indicators are influenced by outside factors and without additional analysis do not provide meaningful measures of effectiveness. For example, the tax-change-per-audit-day indicator is heavily influenced by inflation, economic growth and tax rate increases. Departmental data showed a large increase of 150 percent in this indicator from 1974 to 1988. However, when we adjusted it for inflation, one of the many external factors, we found that it had decreased by about 5 percent in that time. There has also been an absence of analysis on the effect of taxpayers' compliance behaviour on this measure. Research and analysis could also be carried out with a view to identifying high-risk industries or commodities, to guide deployment of scarce enforcement resources.

18.87 In the remaining days of the current system, the Department could build on its existing resource base for research and analysis. This research capacity could then be transferred to the new tax regime. It could also serve as the basis for a functional group to develop ongoing qualitative indicators at that time.

18.88 The Department should strengthen the research and analysis capacity within the Excise Branch. The function should research and analyze program data to identify issues that should be brought to management's attention and to support the Branch's resource allocation strategy and other management decisions.

Department's response: *The Department agrees that a research and analysis capacity within the Excise Branch is important. Although the Branch did not have a discrete unit, such analysis has been employed to identify issues for resource allocation strategies and decisions. However, it will not be possible to build on the former base at this time. Rather, resources are being deployed to GST implementation, leaving a reduced Headquarters complement to deal with ongoing FST matters.*

GST Implication

18.89 Performance information will continue to be a major issue after the introduction of GST. In addition to developing quantitative measures, the Department will need to consider the qualitative dimension. To manage the new tax regime, it will be essential to have the capacity to identify emerging issues and a framework for monitoring compliance and progress of program delivery on an ongoing basis.

Excise program data collection and the sharing of information among functions could be improved to make administration more effective

18.90 We found that certain program data have not been collected; for example, information on refund claims, which represent a major drain on enforcement resources and a vulnerable point for revenue leakage, is very limited. Refund claimants are not required to identify directly whether they are licensed. If the Branch had this basic information, it could identify refund trends for licensees from particular industries to focus verification efforts. Data on non-licensed refund claimants could be screened and referred to the licensee identification function for follow-up if appropriate. In addition, the reason for the refund claim is not categorized. This information would have given the Branch an opportunity to identify possible weaknesses in legislation or interpretation which could result in revenue loss. Where refunds are denied, the reason is not categorized, although this could highlight areas where information services to taxpayers ought to be improved. Furthermore, the refund function is not computerized, making data analysis difficult even if the data had been collected. This would have been done as part of the Excise Commercial System (ECS). However, this part of the ECS development was cancelled as a result of the budget announcement.

18.91 We also found that there has been insufficient sharing of information among functions. The appeals sub-activity, introduced in 1985-86, is a quasi-judicial function which provides an independent review of assessments contested by taxpayers. The sub-activity maintains operating statistics on volume, caseload and cases upheld, varied or overturned. Summary statistics have been provided to the regions; however, information on the reasons for varied or overturned assessments has not. This could provide insight into tax interpretations, rulings weaknesses and vulnerable audit practices and could possibly lead to the policy and system staff discussing amendments to the legislation with the Department of Finance. We also noted that Excise regional directors only receive performance data pertaining to their respective regions and the national statistics. The sharing of information among regions could also highlight issues at the regional level.

18.92 The Branch's mandate is to deliver a single program activity. All sub-activities are directed to achieving the objective of assessing and collecting federal sales and excise taxes and fostering voluntary compliance. It would therefore be logical for these sub-activities to integrate and share program data to enhance the Branch's program delivery.

18.93 The Department should develop better procedures for collecting, analyzing and sharing data for the Excise program to improve the effectiveness of its FST administration.

Department's response: *We agree. Collection and analysis of data would be greatly enhanced with the aid of computers. Related enhancements to the recently implemented Excise Commercial System for FST must be withheld in view of the need for redeveloping the system for GST implementation. However, we have plans to develop and implement an Early Warning System within the Tax Interpretations function in 1989-90. This system is intended to analyze reasons for appeal decision and for tax changes made by audits to identify areas where departmental information could be improved.*

GST Implication

18.94 With a minimum of a 13-fold increase in the population of taxpayers and only a possible two- to three-fold increase in staff, proper data collection and analysis will be essential for effective delivery of the new GST program. The Department will need to integrate and share information among Excise sub-activities and regions to put the data to the best use. In addition, appropriate computer system support will be required to process the anticipated high volume of FST rebates described in paragraphs 18.44 to 18.46.

Administrative Practices -- They Have Gone Beyond Legislative Authority

18.95 In paragraph 18.51, we pointed out that the FST system, introduced in 1924, has not kept up with the current business environment. Over the years, the Branch has developed a network of administrative practices in an attempt to compensate for this. The April 1989 budget documents indicated that "no fewer than 22,000 special provisions and administrative interpretations have been required to achieve some equity under a basically inequitable tax". Many of these special arrangements have not been supported by legislative authority.

18.96 The Department advised us that the Branch has used these administrative practices for two reasons -- to provide greater taxpayer equity and to facilitate the application of the law in complex situations.

18.97 However, in our opinion, the administration of the statutes should be within legislative authority. When administrative practices and interpretations are beyond the law, the Department operates beyond its mandate and, effectively, sets government policy. In addition, it leads to:

- difficulty in maintaining consistency in rulings and interpretations;
- compromising the government's revenue position and the basis for taxpayer appeal; and
- information on administrative practices not readily available to all taxpayers.

All of these problems could cause unfair treatment of taxpayers, higher compliance costs because of the proliferation and complexity of the special provisions, and revenue loss.

Administrative practices have made it more difficult to maintain consistency in rulings and interpretations

18.98 The FST system has numerous exemptions. This, coupled with the broad definition of manufacturing and producing activities, invites taxpayers and their consultants to challenge borderline cases, to minimize their tax liability. In these circumstances, it is inherently difficult to maintain consistency in the rulings and tax interpretations function.

18.99 We found that administrative practices have exacerbated the problem. Tax interpretation officers have often found themselves interpreting not just the legislation but also the administrative practices, many of which extend beyond the law. Application of these practices has sometimes been arbitrary and inconsistent. At times, the practices have also had to be broadened in an attempt by the Branch to be fair to other taxpayers.

18.100 The aggregation policy on certain construction equipment is an example. The Act exempts certain construction equipment and related repair and replacement parts from tax if the fair sale price by the Canadian manufacturer or the duty paid value of the imported unit exceeds $2,000. In an attempt to provide greater equity to taxpayers, the Department has adopted a policy that extends the exemption to include the aggregated value of component parts forming an assembly designed for the exempt equipment, if it exceeds the $2,000 threshold.

18.101 We found inconsistent applications of this policy by different regions. Some interpreted it liberally and extended the aggregation concept to the costs of repair parts; others did not. The inconsistency did not come to the attention of the Department until a taxpayer complained to the Minister of National Revenue. This led to the announcement of a new departmental policy, which brought about a flurry of refund claims. The policy granted the liberal interpretation for the period during which inconsistent rulings had been issued by different regions, and reverted back to the original position as at the announcement date. The Branch estimated payout totalling some $20 million.

Administrative practices compromise the revenue position and do not provide a basis for taxpayer appeal

18.102 Administrative practices that are outside the legislation may not be defensible in a court of law. Thus, any policy which imposes a tax that is more stringent than the legislated liability will not be viable; the taxpayer can simply comply with the legislation rather than the administrative practice. As a result, such administrative practices are generally a liberalization of the law and effectively compromise the revenue position of the Crown. In addition, taxpayers cannot appeal against unfair treatment and application of the practices.

18.103 The notional values system is a prime example of an administrative practice outside the law. The system has a long history, dating back to the 1920s. It was developed to provide a more equitable tax treatment when a manufacturer sells to more than one trade level and to simplify the method of determining the base for sales tax calculation. The Excise Tax Act sets the sales price as the basis for tax. The system offers two alternatives to this -- established values and determined values. Established values are set by taxpayers on the basis of prices used in regular sales to bona fide independent wholesalers or retailers. Determined values are set by the Branch according to industry, and are usually based on market surveys.

18.104 The application of determined values has benefitted taxpayers, as taxes have been computed on a value that is less than the sales price. Further, the values system has been costly to maintain; it is generally time-consuming to conduct market surveys. To the extent that some of the existing determined values are out of date, this could result in further revenue loss. One of the existing circulars on values dates back to 1959. The Branch has been updating some of its determined values. In view of tax reform, the Branch plans to discontinue other updates.

18.105 Further, since the values system is entirely outside the legislation, taxpayers have no legal recourse. This has resulted in an anomaly in tax administration, as interpretations of legislation are subject to appeal through the courts or an independent tribunal. We noted this in our 1979 Report and recommended that the system be codified. The Branch advised us that there had been several discussions with the Department of Finance on the introduction of legislative amendments but they had not been successful. This anomaly has remained in the FST administration.

Information on administrative practices may not be readily available to all taxpayers

18.106 The Branch's policy statements and administrative practices are promulgated through a wide range of publications, including the Excise News, Excise Communiqués, Excise memoranda on policy statement (ET/PS) and Excise operating memoranda (ET/OM). There is also an electronic database of rulings known as RISE, operated by a private firm which provides on-line access for a fee. In addition, Tariff Board and other court decisions form a valuable source of information. The photograph displays the Excise Tax Act and a number of sources of administrative policy statements.

18.107 Most of the departmental publications, especially the Excise memoranda, have been written by technical staff and have not been edited for general consumption. Sometimes the same subjects have been discussed in different publications, which has not facilitated a ready understanding of the most recent departmental position. The same has been true for the RISE database, which contains over 9,000 rulings, many of which are too specific for general use. Some are also inconsistent or outdated.

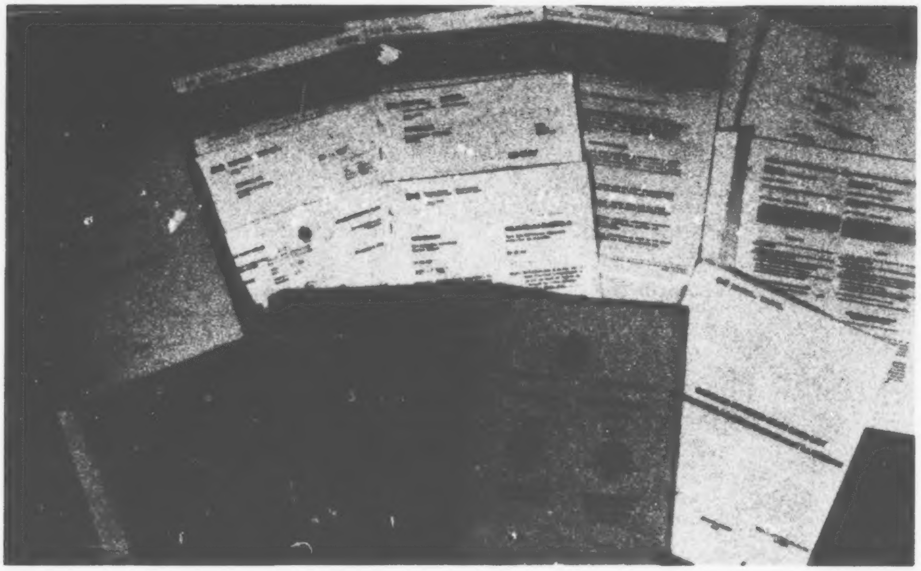
18.108 The Branch told us that many of the Excise memoranda have been updated and work is under way on the remaining ones to consolidate the policy statements and make them more understandable. We also noted that it has tried to contain the risk of inconsistent rulings and interpretations. During our audit, head office had begun to strengthen its monitoring role. Controls over the input to the RISE system have also improved and recent updates included a more thorough search of the database to purge outdated or conflicting rulings. We support the Branch's initiative to improve its control over maintaining consistency of rulings and interpretations and reduce the risk of tax leakage.

18.109 However, except for large licensees who have in-house expertise, most taxpayers need to rely on expert advisers for information on current practices and the implications these have on their tax liability. For example, despite efforts by the Department, not all taxpayers have known about the notional values system and how to apply it to their business. This has given an unfair competitive edge to those who know and use it.

18.110 Furthermore, the growth of administrative practices has imposed additional compliance costs on FST taxpayers. They need to keep abreast with current practices and comply with them. This requires them to staff more in-house expertise or to use sales tax consultants to help them to comply.

GST Implication

18.111 We noted the high risk of inconsistent treatment of taxpayers, higher compliance costs and revenue loss resulting from administrative practices outside the law. In view of this risk, we are of the opinion that under the new tax regime the Department should restrict its administrative practices to interpretations of the law and keep special arrangements and provisions to a minimum. In addition, it should keep its administration simple to reduce taxpayers' compliance costs.



The photo shows the Excise Tax Act and various sources of departmental policies and administration practices needed for taxpayers to comply with the FST administration (see paragraph 18.106).

Tools and Training -- Opportunities for Improvement

18.112 Tools and staff training are important components of an efficient and effective operation. For the tax interpretations and verification and enforcement sub-activities, there are opportunities for improvement.

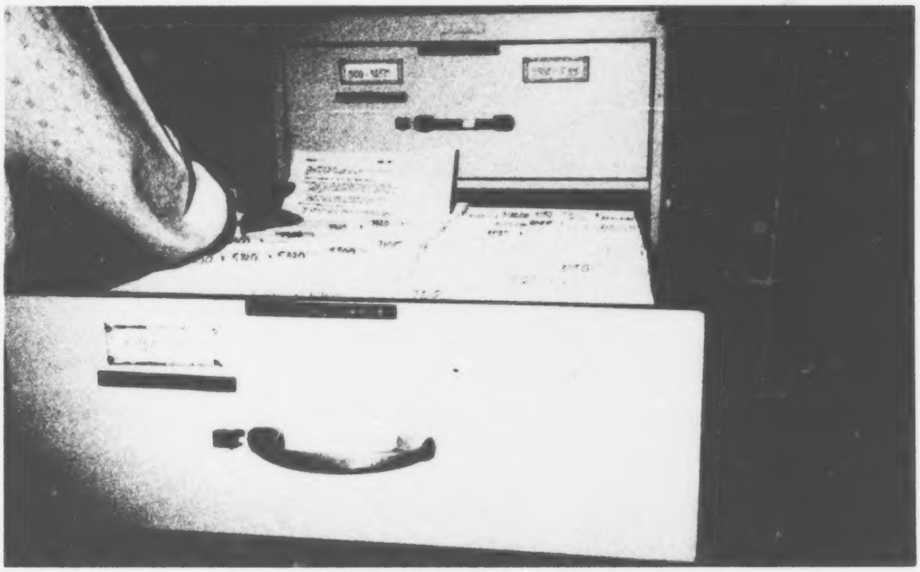
Technical information support to tax interpretations officers and auditors could be improved

18.113 The on-line RISE system is the database for all policy and precedent setting rulings and thus is a key reference source for the staff. This system was developed in the early 1980s and was intended to serve Excise tax interpretations officers and auditors. Since then, it has also been made available to the public, providing on-line access to rulings information at their own cost.

18.114 We believe that this technical information support to Excise staff requires improvement. In our regional visits, we noted that RISE has been used by most tax interpretations officers but rarely by auditors.

18.115 The RISE system is not user-friendly and requires training and practice before it can be used effectively. Although most tax interpretations officers have had training in conducting searches on the system, most auditors have not been trained. Of those who have had the training, some have not had the opportunity to practise using the system because of equipment shortages. Tax interpretations officers have had more access to the system and are using it more frequently. Although regional offices have the equipment to access the RISE system, it does not appear to be adequate. Moreover, the Branch has not withdrawn the duplicate manual ruling card system, and a large proportion of the staff has continued to refer to it instead of RISE. The photograph below shows the manual system with over 9,000 ruling cards. Although the RISE system has been in place since 1982, there has still not been a plan to phase out the manual system.

Many Excise staff have continued to use the duplicate manual ruling card system instead of the on-line RISE system (see paragraph 18.115).



18.116 Not only is it costly to maintain both the computerized database and a parallel manual system, but the existence of the manual system also detracts from the use of the more efficient information support system. In our opinion, it is also imperative to provide reliable and unrestricted access to the equipment to achieve full benefits from the RISE system. Investments in hardware and improved staff skills in conducting computerized searches will also have payback under the new tax system.

18.117 In internal correspondence dated 2 December 1988, the Department raised the possibility of reducing the number of sets of cards in the manual system or eliminating them entirely. We were advised by the Department that the Halifax and Ottawa offices had withdrawn the card system. Since then, the Department has advised us that it will be reduced to a backup system for RISE. The Department is also acquiring more microcomputers which can be used to access this on-line system.

18.118 The Department should expedite its plan to reduce the use of the manual card system. This should be co-ordinated with an equipment review to ensure that the operational staff will have sufficient access to the RISE system.

Department's response: *The Department agrees that the manual system should be eliminated, and indeed this is the intent. However, in view of the continuing needs for the information, the disruption of preparing for GST and the minimal costs of maintaining the card system, it would not seem appropriate to launch a further special initiative at this time. We will continue procedures implemented in September 1988 to speed the input to the automated ruling system. In addition, a comprehensive review of the system is planned to start in October 1989, to recommend improvements and enhancements to ensure accuracy, completeness and relevancy of rulings contained in it. With the continued improvements in and accessibility to RISE, use of the manual system will be gradually eliminated.*

Other tools could improve the cost-effectiveness of the audit function

18.119 At the time of our audit, we noted that most of the Excise audit staff had their own "black book" system of files with Excise memoranda, internal correspondence and rulings from other files or cases as their research base. There is a risk that staff files such as these are outdated or incomplete. They arose as a result of a central research facility that was inadequately equipped and indexed. In addition, the audit staff are not supported with commercially available sales tax reporter services which are often used by licensees and their consultants.

18.120 During our regional visits, we reviewed some audit files and observed the extensive use of hand-prepared worksheets and notes and an absence of computerized working papers. The major use of computers in the audit function has been data retrieval for licensees with computerized records and large volumes of transactions. In this highly computerized era, the Branch is falling behind. Many government organizations and the private sector have proven efficiency gains by capitalizing on technological advances.

18.121 In August 1988, the Branch concluded a review on the use of computers in auditing and recommended that computer acquisition initiatives be funded. The Branch distributed four laptop computers for test use in the regions. As a result of its success, it acquired an additional 150 laptops in March 1989 for the audit function. Near the end of our audit, the Branch had started to train regional staff and to plan for the distribution and use of the laptop computers in the regions.

18.122 In our review of the Excise audit files, we observed that the sampling approach used for audit testing had not been standardized. Some files did not contain proper testing conclusions and some did not document sampling decisions and the reasons for them. In our opinion, a standardized sampling approach is more efficient and can improve the quality of audit testing and its conclusions.

18.123 The Department should explore opportunities to improve audit tools for its staff. It should continue to expedite its plan to introduce laptop computers into the audit function.

Department's response: *We agree. The Department has every intention of acquiring laptop computers as quickly as resources are available. Furthermore, development of other audit tools is continuing, since these initiatives will be equally applicable to GST auditing.*

Roles and responsibilities for training in the Excise Branch are diffused

18.124 In our 1979 report on the Excise Branch, we noted a number of weaknesses in training. Since this 1979 audit, the Branch has developed and started to implement a new Human Resource Management System (HRMS) to integrate the performance appraisal process and the identification of staff training needs. This system has also been used to facilitate the staffing process. It is an innovative initiative and is to our knowledge a unique system in the federal government.

18.125 In the 1979 audit, we also noted that the Department embarked on a project to establish a centralized training college in Rigaud, Quebec to co-ordinate training efforts, eliminate fragmentation, ensure uniform training and reduce the time needed to train staff. Our interviews showed that the college has served primarily as a course site and is functioning as one of many focal points for training Excise Branch staff. The original intent to have the college as the unit responsible for co-ordinating all training matters has not been met and this single co-ordinating role has not been filled elsewhere in the Department.

18.126 The roles and responsibilities for training Excise staff are diffused. In January 1988, Branch management promulgated a statement on training in the Branch. In this statement, training responsibilities were delegated to all head office units and the regions. In particular, the Planning and Administration Division at the Branch's head office was given the responsibility to co-ordinate all Excise training and development activities. It maintains the HRMS system, supports training activities and provides support services to the Human Resource Committee. Although this unit administers the information system and facilitates training, it is essentially an administrative unit and has not been staffed with sufficient pedagogical expertise to assess the adequacy of the Excise training program against changing operational needs.

18.127 There has been no overall task analysis in recent years to enable the Branch to evaluate the adequacy and effectiveness of the existing course curriculum. Updates and development of new courses have been done on an ad hoc basis. The Branch's 1989-90 Training Directive identified that courses representing two-thirds of its training and development expenditures have been in place and operational since 1978, with much of the content and structure unchanged since implementation. The Directive is calling for the review and evaluation of 5 of its 13 core courses in 1989-90.

18.128 We also noted that regional initiatives on orientation and special subject matter sessions are generally not captured by the central unit with a view to sharing them with other regions.

18.129 The Excise Branch has been facing an increasingly complicated environment, with the external pressures which make tax administration more complex. In addition, the Branch has had a high staff turnover rate, particularly the technical staff. In these circumstances, an effective unit to focus training efforts is not only cost-effective but essential.

18.130 The Department should ensure that a functional unit is in place to review existing training courses and regional materials and consolidate training efforts within the Branch with a view to delivering a training program tailored to program activities needed for the remaining days of the FST system.

Department's response: *We agree. The Branch has already reviewed training materials to tailor basic modules to remaining FST activities. In addition, a Branch training co-ordination focus has been instituted at Headquarters, to co-ordinate training plans.*

GST Implication

18.131 Our audit noted some of the same training weaknesses reported in 1979. We are concerned about the training implications of sales tax reform which will involve both the potential two- to three-fold increase in staff and the existing Excise staff. Under the GST, it will be critical for the Department to ensure that there is a focal point for all training matters; including: identifying training needs; ensuring proper course design and development; co-ordinating course delivery; and; monitoring and evaluating training activities.

Transitional Period -- Maintaining the Old System While Preparing For the New Tax Regime

18.132 The FST system remains in effect for 20 months from the announcement date. During this period, the government will continue to rely on it as a major source of budgetary revenue. In fact, effective 1 June 1989, the FST rate for general taxable goods increased by 1.5 percent to 13.5 percent to provide an additional $1.6 billion of government revenue in 1990. Hence the Department must be vigilant in safeguarding the system, and must not permit the period to be seen as a tax holiday. In our view, in addition to maintaining ongoing Branch operations, there are two issues that the Department should consider during this transitional period -- a major tax avoidance mechanism and a close-out strategy.

The use of marketing and distribution companies has been a major tax avoidance mechanism

18.133 The Branch and the Department of Finance recognize that certain taxpayers have been eroding the tax base by diverting their marketing and distribution (M&D) costs to separate companies. The government brought forward proposals on a number of occasions to deal with the problem. The latest proposal, announced in the February 1988 budget, was withdrawn in April 1989 when the GST announcement was made. In an August 1987 Finance and Economic Affairs Committee hearing, the Department of Finance noted an estimated revenue loss to date of about $1 billion to $1.5 billion. In the April 1989 budget papers, the government estimated annual revenue loss of $350 million as a result of this tax avoidance mechanism.

18.134 The withdrawal of the proposed interim sales tax measures has meant an open invitation to taxpayers to use M&D companies to reduce their tax base. However, there are costs associated with setting up affiliated M&D companies, and potential income tax implications, both of which offer some deterrent effect. Since the Department of Finance has been involved in proposing to amend legislation, we have not seen a concerted effort by the Branch to ensure that such taxpayers have set up their M&D companies properly and have set out defensible transfer pricing. In our opinion, this should be included in the Department's enforcement strategy to provide some deterrent effect against tax avoidance.

A close-out strategy will be necessary

18.135 After the new GST comes into effect, the Department will have up to four years to reassess taxes under the FST system. The Department will have to decide how it chooses to wind down its FST administration.

The Branch must prepare itself and prospective taxpayers for the new Goods and Services Tax implementation.

18.136 The transitional period and the four following years provide the last opportunity for the Branch to audit licensees and assess the amounts of FST that should have been reported and paid. The Branch has a number of options. These include keeping to its regular enforcement program; integrating close-out audits with the verification of FST rebates or the introduction of GST to taxpayers; and conducting stand-alone close-out audits. A strong close-out strategy and efficient deployment of resources will be necessary.

18.137 While the Branch maintains the FST system, it must prepare itself and prospective taxpayers for the new GST implementation. Further, existing weaknesses and problems will have to be analyzed and corrected for the new tax administration. Management and staff must all work together to meet this challenge and support the government's major initiative of sales tax reform.

19

DEPARTMENT OF NATIONAL REVENUE - TAXATION

Revenue Programs and Source Deductions

19

DEPARTMENT OF NATIONAL REVENUE - TAXATION

Revenue Programs and Source Deductions

Main Points

19.1 Millions of dollars in additional revenues could be collected if National Revenue - Taxation were to expand its payroll and non-resident audit coverage further. This is demonstrated by the fact that increases in audit coverage since 1984-85 have resulted in substantial increases in source deductions assessed and in the amount of unreported income discovered (paragraphs 19.37 to 19.44).

19.2 Delays in the receipt and deposit of revenues due to National Revenue - Taxation's processing procedures have been reduced following interim changes made by the Department in 1988. These delays were highlighted in a 1986 study commissioned by the Office of the Comptroller General and were estimated by us to cost roughly $24 million annually. Final measures instituted in early 1989 to speed the deposit of cash received through district offices should further reduce or eliminate this cost (19.20 to 19.22).

19.3 Productivity levels differ in taxation centres for similar activities. The differences result from a variety of factors, many of which can be influenced by departmental management alone or in concert with the central agencies. Analysis of these activities would likely reveal opportunities for efficiency enhancement (19.71 to 19.78).

19.4 In the event of a disaster, National Revenue - Taxation does not have an adequate plan for continuing operations on an interim basis while the computer system is being restored (19.32 to 19.34).

19.5 Problems that we have reported on two previous occasions (1985 and 1987) concerning the growth of the Canada Pension Plan unidentified earnings file have not yet been resolved. The value of items in the file has now reached $108 million. If contributors do not receive credit for these contributions, their pensions will be lower than they should be (19.60 to 19.63).

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DEPARTMENT OF NATIONAL REVENUE - TAXATION

Revenue Programs and Source Deductions

Introduction

19.6 The Department of National Revenue - Taxation collects four main categories of revenues: federal income taxes, provincial and territorial income taxes where determined by agreement, employer and employee contributions to the Canada Pension Plan, and employer and employee Unemployment Insurance premiums. The following table shows the amounts collected in the 1987-88 fiscal year.

	Gross Collections 1987-88
Federal Income Tax	$ 68,301,605,000
Provincial Income Tax	20,367,174,000
Canada Pension Plan Contributions	5,583,236,000
Unemployment Insurance Premiums	$ 10,670,769,000
Total Revenues	$ 104,922,784,000

(Source: Report of the Department of National Revenue - Taxation for the fiscal year ended 31 March 1988)

19.7 **Source deductions.** When Canadians file their income tax returns each spring, they have often paid all or part of their taxes, Canada Pension Plan contributions, and Unemployment Insurance premiums through deductions made by their employers from their incomes. Employers remit these funds to the Department of National Revenue - Taxation at least once a month. All such remittances are recorded on computer files. Later they are allocated to the appropriate individual taxpayers' records, which are also maintained on computer files.

Number of taxpayers with source deductions in 1987	13,418,133
Number of active employer accounts with the Department of National Revenue - Taxation at 31 March 1988	1,233,727
Total source deductions for the fiscal year ended 31 March 1988	$ 76,662,720,000

19.8 **Instalment payments.** Some types of income are not subject to deductions at source, including alimony and maintenance payments, certain tips and gratuities, interest, dividends, rental and investment income, self-employment income, and some pension payments.

19.9 Most individuals are required to make quarterly instalment payments of income tax unless tax is deducted at source from at least three-quarters of their net income, or their net federal tax payable for the current or preceding year does not exceed $1,000. Farmers and fishermen whose tax for each of the current and preceding years is more than $1,000 pay instalments on a different schedule than other individuals.

19.10 Corporations remit income tax in monthly instalments.

19.11 Payments on filing. When individual taxpayers file their income tax returns, many will have a balance owing. They are required to remit the balance by 30 April. Corporate taxpayers are required to remit balances owing two or three months after their fiscal year end, depending on the type of corporation.

19.12 Non-residents. Individuals who are not resident in Canada must pay non-resident tax on certain income from Canadian sources. This tax is required to be withheld at source.

Source Deductions and Revenue Programs Activities

19.13 Receipt, deposit, and accounting for revenues. Revenues are received in financial institutions, taxation centres, and, increasingly, in district offices. They are deposited to the credit of the Receiver General for Canada in various financial institutions and subsequently transferred to the Bank of Canada. Within National Revenue - Taxation they are accounted for in a number of computerized systems.

19.14 Inquiries and correspondence. District office staff provide information and answer general questions pertaining to source deductions. Taxation centres are responsible for answering correspondence concerning employers' and taxpayers' accounts.

19.15 Audit and enforcement. The Department monitors amounts received from employers, to identify those who have not deducted or remitted as required. It contacts delinquent employers to request payment and, if necessary, audits their records and issues assessments for the amounts due. It may also audit employers to uncover unreported employment income and taxable benefits given to employees, or to verify deductions of Canada Pension Plan contributions and Unemployment Insurance premiums from pensionable and insurable earnings. The source deductions program also conducts audits of payments made to non-residents to uncover those that are subject to non-resident tax.

19.16 Canada Pension Plan and Unemployment Insurance. The Minister of National Revenue - Taxation is responsible for administering certain aspects of both the Canada Pension Plan (CPP) and the Unemployment Insurance Program (UI). The Department of National Revenue - Taxation collects contributions, premiums and benefit repayments, gathers certain information, and issues rulings on the application of certain provisions of the relevant legislation. Amounts collected and information gathered are transferred to the departments with primary responsibility for CPP and UI administration.

Audit Scope

19.17 We defined our scope to be the activities under the functional direction of the Source Deductions and Revenue Programs Divisions which, together with the Collections Division, make up the Head Office Collections and Accounting Directorate. The Collections Division was the focus of a chapter in our 1988 Report. The responsibility for operations lies with the five regional offices -- and the 37 district offices and seven taxation centres that report to them. We carried out our audit of the operations in a sample of two regional offices, seven district offices, and four taxation centres across Canada. In our view this sample represented a reasonable cross section of the Department.

19.18 Source Deductions and Revenue Programs are supported by certain computer applications operated by the Head Office Information Systems Directorate. We examined these applications.

19.19 Some of the activities included in our scope had been examined by the Department's internal auditors within the last three years. We reviewed the internal audit reports and followed up some of the findings in the course of our audit.

Revenue Programs

Cash Management

19.20 Given the enormous volume of receipts that National Revenue - Taxation handles, it is important that processing at all stages be done efficiently to minimize the associated financing costs. Amounts received by National Revenue - Taxation, but not yet deposited to the credit of the Receiver General for Canada with the Bank of Canada, are referred to as the "float". The term "financing cost" is used in relation to the amount of this float. Until amounts have been deposited to the credit of the Receiver General for Canada, the government does not have use of the funds. We assume that the government would have reduced the amount of its borrowing by the amount of these funds. The term "financing cost", therefore, refers to the interest payable on an amount of borrowing equal to the amount of the float.

The processing of remittances made to district offices is more efficient

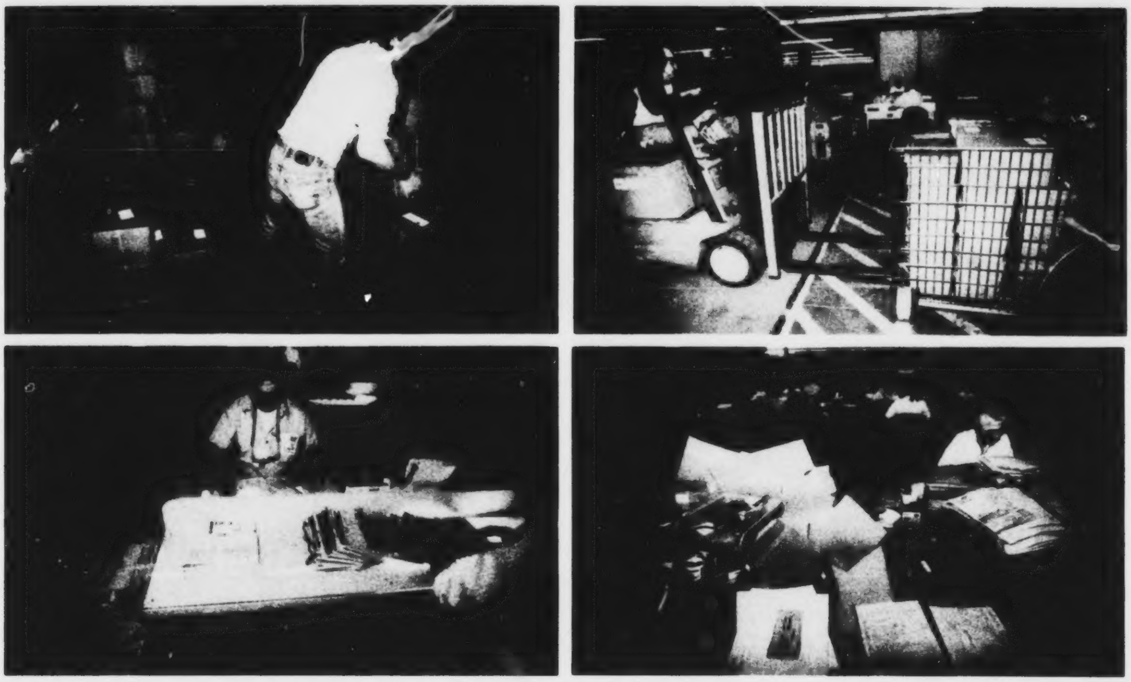
19.21 Until very recently the Department's deposit-making function was concentrated in the taxation centres. Amounts received by district offices were forwarded to the nearest taxation centre for deposit. Statistics developed by National Revenue - Taxation show that it took an average of three days for the receipts to travel from a district office to a taxation centre. Since district office remittances averaged $80 million a day, this created a float equal to three times that amount, or $240 million. The annual financing cost of carrying the float would be $24 million at an assumed interest rate of 10 percent.

It is important that cheque deposit and other processing be done efficiently to minimize financing costs.

19.22 A study dated October 1986 commissioned by the Office of the Comptroller General highlighted this delay. As an interim measure, district offices began in June 1988 to deposit cheques having a large value, thus reducing the financing cost by half. The study also became the impetus for National Revenue - Taxation's "District Office Cash Project". Under procedures implemented in early 1989, district offices themselves make deposits of all amounts they receive. This should greatly reduce or eliminate the former delay.

Processing of payments included with tax returns has improved substantially in 1989

19.23 Individual taxpayers having a balance of income tax owing tend to delay filing their returns until the 30 April deadline. This creates a peak workload for National Revenue - Taxation as returns with payments enclosed flood in during the early days of May each year.



Taxpayers with balances of income tax owing tend to delay filing until near the 30 April deadline. This creates a peak workload for the NR-T cash receipts processing system as returns with payments enclosed flood in during the early days of May each year (see paragraph 19.23).

19.24 In 1988, it took until 27 May for the Department to deposit all these payments. It estimated the financing cost of the delay in depositing to be about $3.4 million.

19.25 In October 1988, the Department set out to develop strategies that would enable it to clear the backlog of payments on filing more quickly. The target for 1989 was to clear the backlog by 19 May at the latest. This was expected to reduce the financing cost to $2.3 million, an improvement of $1.1 million. All taxation centres met the target, and one taxation centre was able to clear the backlog by 9 May 1989. The Department plans to review and evaluate the methods used to achieve this performance.

Delays in depositing certain receipts result in failure to comply with legislative requirements

19.26 Regulations made pursuant to the Financial Administration Act require the deposit of amounts received each day, unless the total is less than $500. Paragraphs 21 to 25 indicate that National Revenue - Taxation has not always complied with this requirement. The Department believes the legislative requirements cannot be achieved as they apply to payments on filing.

The Department does not have the information necessary to determine whether the processing of remittances through "indirect clearers" is cost-effective

19.27 Employers may deliver the amounts they have withheld from employees, together with their own contributions and premiums, to any financial institution. Individuals and corporations may make their income tax instalment payments in the same way. Some financial institutions, called "direct clearers", have agreements with the Receiver General for Canada under which they charge for each remittance they process and pay interest on amounts they have received but have not yet credited to the Receiver General. Other financial institutions, called "indirect clearers", receive no service charges and pay no interest.

19.28 Indirect clearers typically use the mail to transfer to National Revenue - Taxation the amounts they have collected. Statistics developed by National Revenue - Taxation for the period from September 1988 to March 1989 show that the average difference between the date remittances were received by a financial institution and the date they were received by the Department varied from 7.59 to 8.98 days. The overall average was 8.16.

19.29 The average daily amount of remittances transferred by indirect clearers through the mail during this period was approximately $1.3 million. The annual financing cost of carrying a float equal to eight days' remittances is $1.0 million at an assumed interest rate of 10 percent. The Department does not know the value of service charges that would be required to pay indirect clearers on the same basis as direct clearers. Consequently it is unable to assess the cost-effectiveness of processing through indirect clearers. Late in 1988 information to perform the analysis started to become available and when sufficient data are available the Department of Supply and Services will proceed with a cost-benefit analysis.

Cash Receipts and Accounting Systems

19.30 The cash receipts and accounting systems at National Revenue - Taxation consist of both manual and computerized processes. Transactions are initially recorded in the Financial Information Processing System, which sorts the transactions and channels them into other subsidiary systems and the Department's general ledger. Subsidiary systems include those that maintain individual taxpayer accounts, corporate taxpayer accounts and payroll deduction accounts.

19.31 In view of the amounts of revenue that the Department handles, it is essential that there be a sound system of internal controls over cash receipts to protect against loss through fraud or error. We reviewed documentation and made inquiries concerning certain key internal controls and found no evidence of significant deficiencies. However, we did not test the controls to determine whether they were functioning as intended. The Department's internal auditors periodically test the procedures performed at each taxation centre.

The Department has not made adequate arrangements for recovery of its cash receipts accounting systems in the event of a disaster

19.32 The Department is vitally dependent on its computerized systems. A 1987 internal audit report stated that it did not have an adequate disaster recovery plan. In response to this criticism, the Department has taken some initial steps. A back-up site has been prepared in the Sudbury Taxation Centre to receive computer and telecommunications equipment when required. The area is equipped with the appropriate electrical, air conditioning and fire extinguishing systems while it continues to be used for clerical operations. The Department estimates that it would take about 60 days to get the back-up site operating.

19.33 The disaster recovery plan assumes that the data available in off-site storage will be adequate as a basis for recovery. At the time of our audit, we found that there were not adequate data available off-site. However, the Department has informed us that it has now corrected the situation. We also noted that, except for procedures for manual preparation of deposits, the Department has no plan for operating during the period that it would take to get the back-up site operating.

19.34 The Department should include in its disaster recovery plan a strategy for operating from the time a disaster occurs until the back-up computer site is ready for use. It should also periodically conduct tests to ensure that data maintained in off-site storage are adequate to effect a recovery.

Department's response: *We agree and our EDP Systems and Technology Branch will be convening a Disaster Recovery Steering Committee and a Disaster Recovery Working Committee to address elements of the Disaster Recovery Plan such as the capability to operate following a major shutdown of the main system.*

The Department's systems for performing interest calculations need revision

19.35 Income tax legislation establishes a variety of circumstances in which the Department either charges or pays interest. Responsibility for performing these calculations falls under Revenue Programs.

19.36 Calculation of interest can be very complex. For individual taxpayers, calculations are performed chiefly through the computer software system that maintains individual taxpayer accounts. This system, known as CINDAC, was developed about 25 years ago and has since undergone continuous amendment. As a result, it has become increasingly inefficient and expensive to maintain and modify. The difficulty with interest calculations is simply one consequence of using the software system in its present form. The Department has begun a process of completely rewriting the CINDAC system software over a period of five years with a view to improving its efficiency and capabilities. It plans to complete the segments of the system for performing interest calculations by 1991.

Source Deductions

Audit

19.37 The Source Deductions activity includes four types of audit; three of these are payroll audits and the fourth is non-resident audit. Each year a plan is developed for each type, with a target number of audits to be performed and an allocation of person years to be devoted to the task.

To decide on allocation of its resources, the Department designates its activities as mandatory or non-mandatory. Most source deductions audits are non-mandatory.

19.38 One of the payroll audits is known as an enforcement audit. It is initiated, for example, when National Revenue - Taxation's computer system identifies a potential problem with an employer such as an overdue payment. A second type, known as a service audit, is done after a receivership or bankruptcy where a proof of claim must be filed. The third type of payroll audit deals with unreported employment income or taxable benefits. This is known as a benefit and employment income audit (BEIA). In the fourth category, the non-resident audit, auditors look for taxable payments to non-residents.

The performance of the Source Deductions audit function has improved over the last five years

19.39 A dramatic improvement in the performance of the Source Deductions audit function occurred when the Department allocated more person-years to it. In the year ended 31 March 1985, the total number of audits performed was just over 54,000, some 20,000 fewer than the budgeted number of audits for the year. For the year ended 31 March 1989, the total number of audits performed had risen to over 82,000, only about 2,000 fewer than the amount budgeted for the year. All four types of audit showed increases, but enforcement audits -- with an increase of 17,000 -- and service audits -- with an increase of over 7,000 -- accounted for 85 percent of the improvement.

19.40 This expanded audit coverage has translated into an increase in the additional source deductions assessed of from about $145 million in 1984-85 to $319 million in 1988-89, and in the amount of unreported income discovered of from $35 million in 1984-85 to $82 million in 1988-89. Auditors are also managing to collect a higher proportion of the assessments at the time of their field visits.

19.41 Despite this generally improved performance, the Department has not met its own targets for "percentage coverage" of employer accounts (the proportion audited as a percentage of all accounts) or average age of audit inventory (accounts selected for audit but which have not yet been done). The BEIA and non-resident audits, while increasing in number, have still fallen short of the planned number of audits.

Mandatory workloads divert resources away from audit activities that could produce high returns

19.42 One of the techniques that National Revenue - Taxation uses to rank its assignment of resources involves designating activities as either mandatory or non-mandatory. All Source Deductions audits are non-mandatory, except for service audits. Responding to public inquiries is mandatory. When faced with a pressing mandatory requirement, a manager may shift resources out of a non-mandatory activity into one that is mandatory.

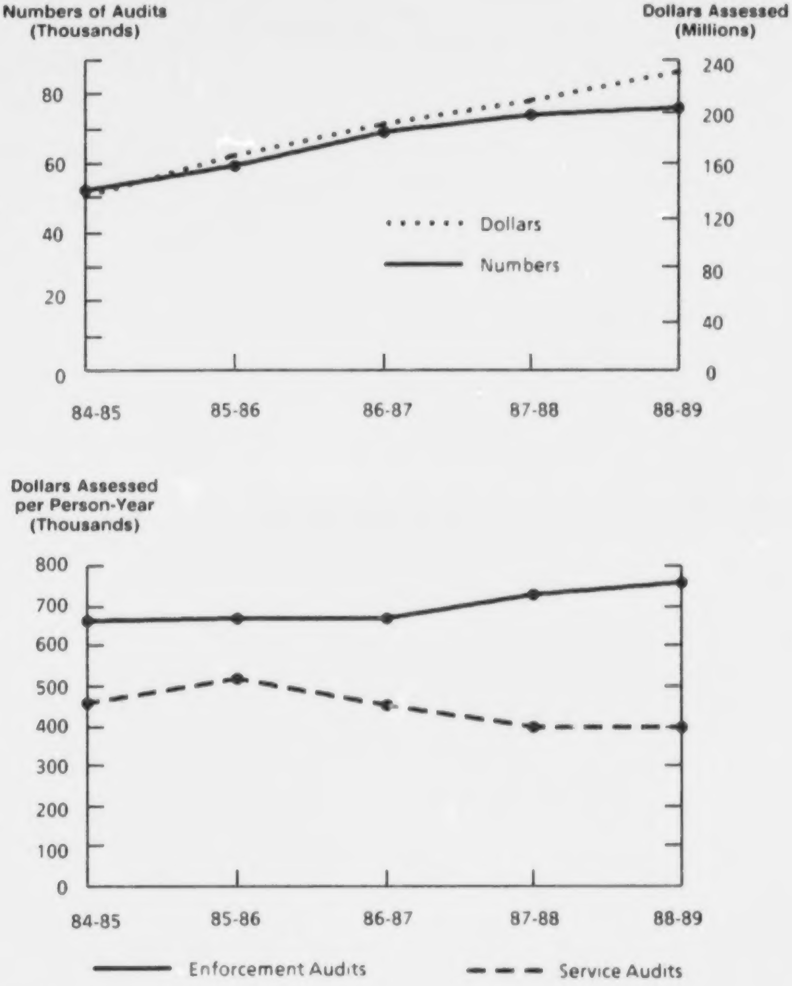
19.43 We noted a few recent instances where resources were temporarily withdrawn from the audit activity and moved elsewhere. Without suggesting that such cases are widespread, we raise the concern that this kind of choice could involve foregoing revenues, particularly where government-wide constraints on person-year resources combine with the Department's current priority of providing service to its clients.

19.44 Statistics show that an additional dollar spent on audit can provide a return of many times that amount. During 1988-89, enforcement and service audits generated revenue in the order of $765,000 and $395,000 per auditor respectively. A typical payroll auditor earned approximately $35,000 annually. It follows, therefore, that millions of dollars in additional revenue could be collected if the Department were to expand its payroll audit and non-resident audit coverage beyond the current level.

19.45 The Department indicated to us that it has recently set up a committee to consider the competing objectives of compliance and service to the public, both of which play a part in its designation of activities as mandatory or non-mandatory.

Enforcement

19.46 The term "enforcement" refers to a variety of follow-up activities on items such as missing remittances of source deductions, missing T4 returns, and discrepancies between amounts received and amounts reported on T4 returns. Enforcement activity is conducted



Improvement in performance of the Source Deductions audit function is observed in increases in number of audits and in revenue from Enforcement and Service audits.

An additional person-year used on Enforcement and Service audits provides a return of revenue many times its cost.

Source: Departmental records

Exhibit 19.1

entirely through correspondence and telephone contact, and is computer-generated. If this is unsuccessful in resolving the problem, the case is referred to audit.

The decision to change a tolerance level was made without the aid of a formal cost-benefit analysis

19.47 To control enforcement workload, "tolerance levels" or cut-off points are established. The computer identifies a problem condition in a particular item, then compares some attribute of the item against the relevant tolerance level. If the value of the attribute is above the tolerance level, enforcement action will be taken, otherwise the problem condition will be ignored.

19.48 The Department recently raised one of its tolerance levels to decrease the workload by 20 percent in that activity; labour hours are also expected to decline. This affects the same activity from which most of the staff resources were taken to handle the rapidly expanding public inquiries function. This is another example of resources being moved from a non-mandatory activity to a mandatory activity.

19.49 In deciding to raise the tolerance level, the Department estimated the amount of resources that would be freed, and reasoned that no significant monetary loss would occur. No formal cost-benefit analysis was done to support the decision. While we do not question the Department's decision, we believe it would be preferable to support such changes with a formal cost-benefit analysis.

The Department's desired levels of voluntary compliance have not been achieved

19.50 Accounts that require some sort of enforcement or audit activity involving personal contact are known as "district office responsibility" (DOR). The Department uses the percentage of accounts that are DOR as one measure of the level of voluntary compliance by employers, setting the goal that not more than 4 percent of accounts should be DOR. Over the past five years, the percentage has often gone over this 4 percent target. In March 1989 it varied from 2.2 percent to 10.6 percent among the district offices, with an average of 4.9 percent. The Department has informed us it will be reviewing the appropriateness of the 4 percent target level and will be seeking to improve the consistency in results.

Inquiries

19.51 In January 1988, responsibility for answering inquiries relating to matters handled by Source Deductions units was transferred from the general inquiries function to the Source Deductions units. It was felt that these inquiries could be handled more effectively by respondents who had greater familiarity with the subject. The change followed two studies by the Department in which concern had been expressed about the quality of information and level of service being provided to callers.

The Department did not accurately estimate the resources required to implement its decision to relocate the Source Deductions inquiries function

19.52 The cost analysis performed considered only the one-time capital cost of supplying telephone stations and the ongoing telecommunications costs. Before the decision, the number of person-years to be transferred from general inquiries to Source Deductions to accommodate the change was not determined. When this was calculated, it was based on historical information, and did not account for certain government initiatives that would cause an increased volume of inquiries. The plan called for 30 person-years to be transferred; in fact a total of 131 person-years was required to handle the volume of calls.

19.53 The Department believes that the quality of responses to inquiries concerning source deductions has improved. However, this cannot be verified because it did not collect the data before and after the transfer which would be necessary to measure improvement. It samples the types of inquiries being handled and plans to do a comprehensive survey of responses to monitor their quality.

The Department cannot in all locations monitor achievement of its level of service targets for Source Deductions inquiries

19.54 The Department has established a level of service standard for telephone enquiries. It requires that no more than 30 percent of callers will hear a busy signal. However, the majority of district offices do not have the equipment to monitor the level of service obtained. A review of the level of service provided through toll-free (1-800) numbers during the period January to April 1989 revealed that 14 offices consistently met the standard, eight sometimes failed to meet the standard, while two consistently failed to meet it. Overall, the standard was not met 28 percent of the time.

19.55 The Department should ensure that district offices have adequate data sources available to permit monitoring of performance standards for the Source Deductions inquiries function.

Department's response: *We agree and have taken steps to acquire the necessary equipment beginning in this fiscal year.*

Accelerated Remittances

The Department has successfully implemented the government policy decision to accelerate source deduction remittances

19.56 Effective January 1988, larger employers who pay their employees at least twice a month must remit source deductions twice a month rather than once. This requirement affects roughly 47,000 employers who, although they make up only 4 percent of the total number of employers, account for about 79 percent of all source deductions collected. The purpose of the change was to improve the government's cash flow, estimating that the effect would be a one-time reduction of about $1.2 billion in the government's annual deficit.

19.57 Cut-off points at which employers would be subject to the new requirement were chosen to minimize the compliance burden on small employers and the administrative burden on National Revenue - Taxation.

19.58 The impetus for the change came from the Department of Finance; National Revenue - Taxation's role was one of implementation. The Department set up a task force to plan and manage the implementation of the change, including a communication program, design of forms, changes to internal systems, and training. It also prepared a contingency plan to cover possible problems or delays.

19.59 Information about the change was sent to all employers in June 1987, more than six months before it was to go into effect. In August 1987 the Source Deductions function sent out a questionnaire to identify the pay period frequency of large employers to enable the Department to adjust its own records to prepare for the more frequent payments. The communication program was generally effective, and minor problems that did occur were promptly recognized and corrected.

Canada Pension Plan

The Department has not worked out an adequate memorandum of understanding with the Department of National Health and Welfare covering its role in administering the Canada Pension Plan

19.60 The Canada Pension Plan (CPP) gives the Minister of National Health and Welfare primary responsibility for the Plan and designates the Minister of National Revenue as the Minister responsible for Part I of the CPP. The Department of National Revenue - Taxation collects contributions, gathers information to be entered on plan members' records of earnings, and issues rulings. (Records of earnings, which are used to determine the level of future pension benefits, are maintained by National Health and Welfare.) Although the two departments share CPP administrative responsibilities, they have not entered into a comprehensive written memorandum of understanding -- despite a recognized need for one -- which defines in detail their specific responsibilities and the manner in which they are to be carried out. The existing two memoranda of understanding of 1986 and 1988 do not address these areas. Although officials of the two departments meet both informally and through formally constituted committees to address many matters, we feel that the absence of an adequate memorandum of understanding is an impediment to the resolution of administrative issues. Two of the more important of these issues, concerning the unidentified earnings file and cost recovery, are discussed in paragraphs 62 to 67.

Four percent of the total number of employers account for about 79 percent of all source deductions collected.

19.61 The Department of National Revenue - Taxation should enter into a memorandum of understanding with the Department of National Health and Welfare that outlines their respective roles in the administration of the Canada Pension Plan.

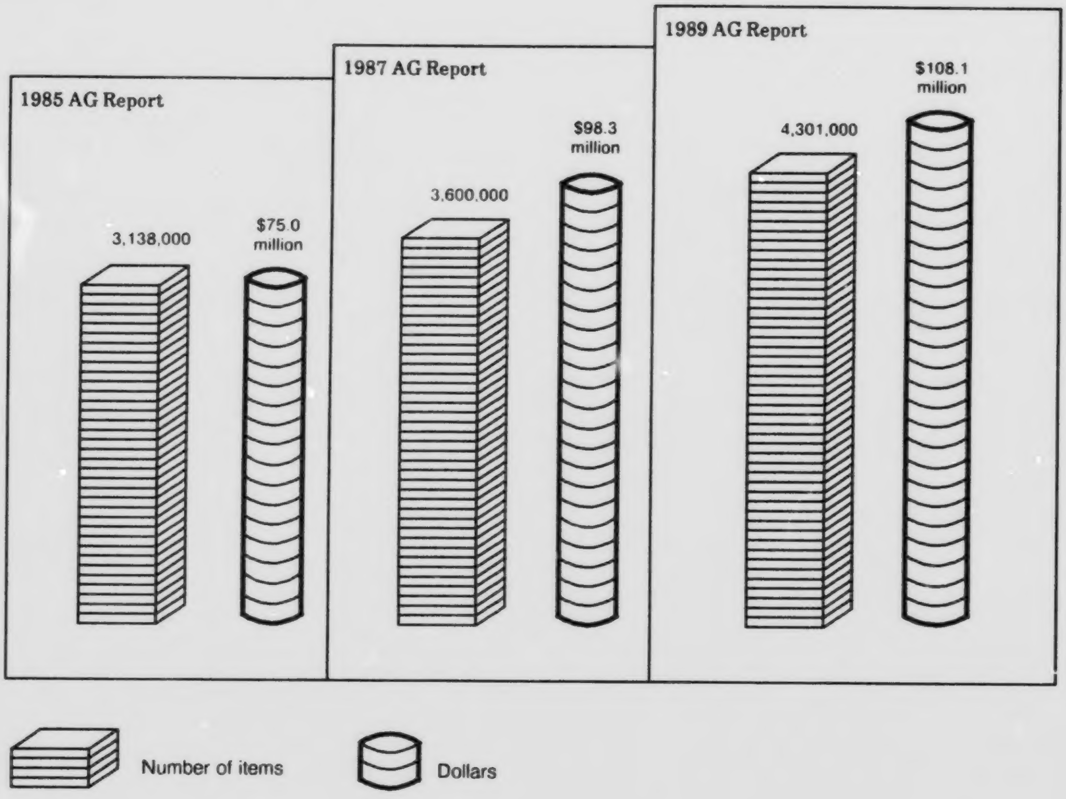
Department's response: *A Memorandum of Agreement was prepared by Health and Welfare and subsequently reviewed by officials of Revenue Canada - Taxation. A meeting was held on 2 and 3 August, 1989 to clarify and revise the proposed agreement to the satisfaction of both Departments. Most of the issues have now been resolved and the final Agreement will be ready in the very near future.*

The CPP unidentified earnings file continues to grow

19.62 Contributions from plan members who cannot be identified are recorded in a series of suspense accounts known collectively as the "unidentified earnings file". Attempts are made to identify the contributors so they can be given credit on their records of earnings. If a plan member does not receive credit for the contributions, the amount of pension that he or she eventually receives will be lower than it should be. Our 1985 Report chapter on Public Pension Management noted that the number of items in suspense was increasing, and our 1987 follow-up chapter stated that the growth was continuing. At the time of this audit we noted that the number of items had further increased and was just over 4.3 million, with a total value of about $108 million (these figures exclude 4.3 million items designated as "meaningless records", which have a total value of under $3 million).

19.63 A study conducted by the Department in 1987 and a report by the CPP Advisory Board in 1988 have recommended various measures to limit the future growth of suspense accounts. Nevertheless, to date there has been no evident success in checking the steady growth of the file. The Department has told us that it is currently devising a plan of action,

There has been no evident success in checking the steady growth of the CPP Unidentified Earnings file. Pension entitlements will be reduced for people whose contributions are contained in this file.



Source: Departmental records

Exhibit 19.2

developing and devising projects, and preparing, for September 1989, a report to senior management of both departments.

The Department has not amended its formula for recovery of costs in respect of CPP in accordance with the Treasury Board's instructions

19.64 The CPP provides for administration costs to be charged to the CPP account. Accordingly, National Revenue - Taxation each year recovers amounts in respect of its cost of providing administrative services to the CPP.

19.65 These are recovered on the basis of a formula approved by the Treasury Board in 1974. Less than two years after the formula was established it became the subject of criticism in an internal audit of CPP operations by National Health and Welfare. The formula, which called for National Revenue - Taxation to allocate costs in proportion to the categories of revenue that it collected, was said to overcharge the CPP. A study by an independent consulting firm was commissioned in 1985; in its 1987 report, it recommended an alternative basis for recovery and showed that, had this method been used, the amount recovered from the CPP for 1984-85 (the base year for the study) would have been roughly $10 million lower than the $45 million actually charged.

19.66 In January 1988 the Treasury Board instructed National Health and Welfare and other participating departments to enter into memoranda of understanding for the 1988-89 fiscal year. These were to ensure that costing criteria and principles for recovering costs were applied as recommended by the consultants. At the time of our audit, the memorandum of understanding between the Departments of National Health and Welfare and National Revenue - Taxation had not been finalized.

19.67 The Department of National Revenue - Taxation should come to an agreement with National Health and Welfare on the appropriate basis for calculating amounts to be recovered by National Revenue - Taxation from the Canada Pension Plan Account.

Department's response: *As a result of a joint submission to Treasury Board, approved on 21 January 1988, Revenue Canada, Taxation and National Health and Welfare agreed to implement a revised methodology for charging C.P.P. administration costs for 1988-89. Indications are that the revised methodology would result in a lower charge of approximately $10 million mainly because the majority of costs of Quebec operations were excluded from the base in the new method.*

Management Systems and Practices

Local Management Information Systems

Efficiency gains may be possible through the standardization of aspects of local management information systems

19.68 Managers at district offices and taxation centres need local systems to supplement the national systems for managing day-to-day operations. Local systems are generally based on microcomputers, and there is a good deal of experimentation as the Department explores the possibilities offered by the advanced technology. Local systems are intended to gather only information that cannot be obtained from the national systems, but some data, such as production volumes and time expended, have to be duplicated.

19.69 Local systems also provide data for the Head Office functional group to incorporate into its quarterly or semi-annual "report cards". Because the local systems are not standardized, this must be manually entered into the Head Office system. There is an opportunity for efficiency gains by standardizing local systems reports so that entry can be done automatically.

19.70 The Department should review local management information requirements and systems so that it can determine which local systems can be standardized for all district offices or taxation centres.

Department's response: *This is an ongoing process and we agree to continue this effort.*

Resource Allocation and Operational Planning

19.71 Resource allocation and operational planning in National Revenue - Taxation occur through a process of negotiation between the Head Office functional group and the regional offices. Each regional office represents certain taxation centres and district offices. Staff from these offices may assist the regional office in the talks. The process promotes higher efficiency in locations whose past results were below the national average, while others must at least maintain their past productivity levels.

19.72 Standards for the next year are derived from past results recorded in the Department's Time Production System (TPS). As a starting point, each location, for a given activity, is asked to at least keep pace with the better of its prior year or current year-to-date results. Those whose results were poorer than the national average will be asked to achieve the national average in the next year. This requirement can be modified in the negotiations to give recognition to a variety of factors that combine to create differences in levels of results. In a taxation centre, for example, these are: the nature, complexity and mix of the workload; the type of workforce; and facilities and equipment. The agreed-upon per-unit standard is applied to the estimated total volume of work for the next year to allocate resources.

19.73 We used 1988-89 TPS data to compare results between taxation centres for an extensive sample of activities, which covered about 1,400 person-years worth of work. We looked at the spread between the results of each taxation centre and the most productive taxation centre for each activity. Adding all activities in the sample, the spread was equal to a usage of 439 person-years. Exhibit 19.3 breaks down the total by taxation centre. However, this figure does not entirely represent potential productivity gains.

19.74 In reviewing our results with the Department, we were told that in some cases the taxation centres were not comparable because units of production, although similar in nature, differed in mix and complexity across taxation centres. Although the Department can't readily quantify the amount, it told us that these reasons explain many of the differences.

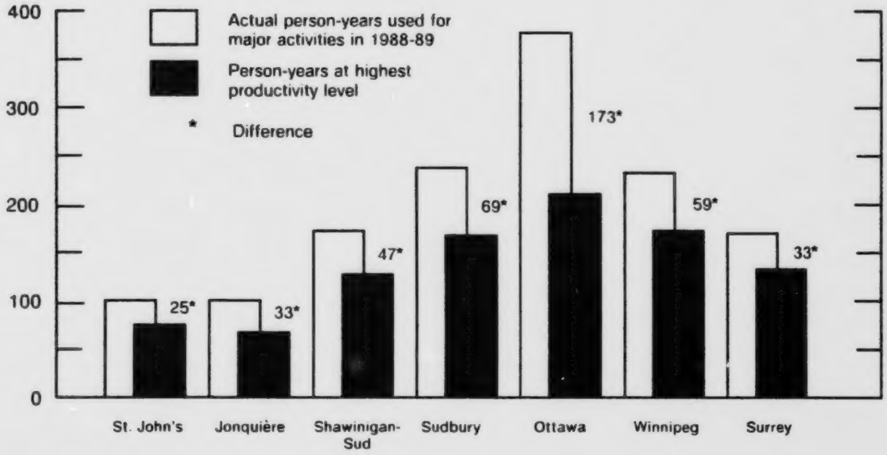
19.75 The Department, where it believes it is appropriate, redefines time production codes and prescribes uniform accounting procedures to give more accurate and comparable data.

Rigorous analysis of operations may identify opportunities for productivity gains

19.76 We believe the differences in results signal the opportunity to enhance productivity -- especially, but not only, among the poorer performers. Even if the potential efficiency gains are only a fraction of the size of the total variation in productivity levels, we think the Department would be justified in using resources to find them. The key lies in the analysis of operations by persons skilled in work simplification and methods improvement to uncover inefficiencies, and in action to achieve improvements. Analysis would also disclose areas where improvements are not feasible.

19.77 Except perhaps for the nature, mix and complexity of the workload, all the factors that cause variations in productivity are controllable over time by departmental management alone or in concert with the central agencies. We are not suggesting that person-year savings from improved efficiency could be achieved overnight, nor do we know what the actual savings would be. But we believe the approach outlined above would be a valuable complement to existing mechanisms that promote greater efficiency.

Differences in the productivity of taxation centres for an extensive sample of activities amounted to the equivalent of an expenditure of 439 person-years.



Source: Calculations based on departmental records

Exhibit 19.3

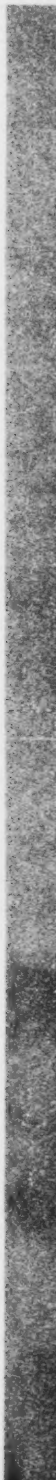
19.78 The Department should, on an ongoing basis, analyze its operations to identify the reasons for variations in productivity, and make changes that will remove revealed inefficiencies.

Department's response: *We spend significant resources on an ongoing basis and will continue to do so reviewing our activities in search of opportunities for improved efficiency. For instance, there are regular departmental meetings, such as the Regional Operations Committees, as well as ad hoc exchanges of information among the various taxation centres, one purpose of which is to foster improved productivity. As well, significant effort is expended in monitoring functional activities at the taxation centres, which can involve reviews by teams of experts (comprised of Head Office and experienced field personnel) looking into opportunities for enhanced efficiency. These processes are complemented by annual report cards prepared by Head Office, which analyze results in the taxation centres, and the more independent internal audits which are conducted by the Department; this information, and any resultant recommendations for changes, are reviewed by the Deputy Minister and the Committee of Revenue Executives (CORE).*

We do not share your view that your study indicates a vast potential for productivity gains since, as was indicated on several occasions, the methodology does not take account of many significant differences in the tax centres themselves and in the specific activities looked at. Nevertheless, the Department agrees with the idea that comparisons should be made amongst the various tax centres, and will continue to review all possible means of making valid comparisons in order to identify potential for productivity improvement.

20

STATISTICS CANADA



20

STATISTICS CANADA

Main Points

20.1 Statistics Canada is a central statistical agency charged with providing statistical information and analyses on Canadian society. Expenditures in 1988-89 were $246.5 million; there were 4,200 full-time employees and approximately 1,600 part-time interviewers (paragraphs 20.8 and 20.9).

20.2 In the areas we examined, we noted a dedication on the part of Agency staff to maintaining good statistical practice. Statistics Canada managers, however, are faced with the challenge of making choices among many competing demands in the context of budgetary constraint. For planning and accountability purposes, more specific information should be included with the statement of activity objectives on the data requirements to meet the needs of the main users (20.17, 20.19, 20.23).

20.3 Statistics Canada's independence in statistical matters is recognized. Its obligation is thus even greater to report to Parliament, through the Minister, and to users of its statistics, the consequences of the choices it makes. More information should be provided on the impacts associated with program changes. An example would be the reinstatement of the 1986 Census with a reduced budget, which resulted in a reduction of the quality of the population count (20.16, 20.44, 20.46).

20.4 Budgetary restraint has resulted in a number of reductions in sample sizes and survey coverage and difficulty in meeting established levels of service to the public. Because objectives were not always clearly defined, the consequences of these changes could not be readily assessed against stated requirements. There is an ongoing need to provide more information to users, for example, on the implications of the changes in the data being put into the System of National Accounts (20.61, 20.66, 20.57, 20.82).

20.5 Steps need to be taken to clearly define the authority under which Statistics Canada is selling publications. We found that the procedure for setting prices of publications was different from that used by the Canadian Government Publishing Centre at Supply and Services Canada. We believe there is a need for appropriate approvals to be obtained for the pricing system for its publications (20.85, 20.88).

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20.1 Program Structure, Budget and Audit Scope 1988-89

20.2 Statistics Canada - Total Operating Expenditures

20.3 Distribution of Statistics Canada Publications 1988-89

STATISTICS CANADA

Audit Scope

20.6 We directed our audit to assessing how Statistics Canada has adapted its practices and programs to budgetary restraint. We selected five statistical programs for examination: the Labour Force Survey; the Annual Survey of Manufactures and the planning of the Business Survey Redesign; the System of National Accounts; Health Statistics; and the 1986 Census of Population. In addition, we examined Marketing and Information Services for statistical products. The audit examined the systems, procedures and management practices in place.

20.7 We did not assess the quality of the Agency's statistical methodology. We used the Agency's own measures of the quality of its statistics to identify the impact of budgetary constraint on programs and practices.

Background

20.8 Statistics Canada is a central statistical agency that has been in operation since 1918. Its broad mandate under the Statistics Act is to collect, compile, analyze and publish statistical information. Decisions made on the basis of this information affect the social and economic affairs of practically all Canadians. Statistics Canada also plays an important role in developing statistical expertise in Canada and abroad.

20.9 The Agency employs approximately 4,200 full-time employees and 1,600 part-time interviewers. The statistics program is divided into six main activities, four broad subject areas and two functional areas that cut across the others (Exhibit 20.1). The Agency also maintains a network of regional offices across Canada which employ over 300 permanent employees and most of the part-time interviewers. Total forecast expenditures for 1988-89 were $246.5 million.

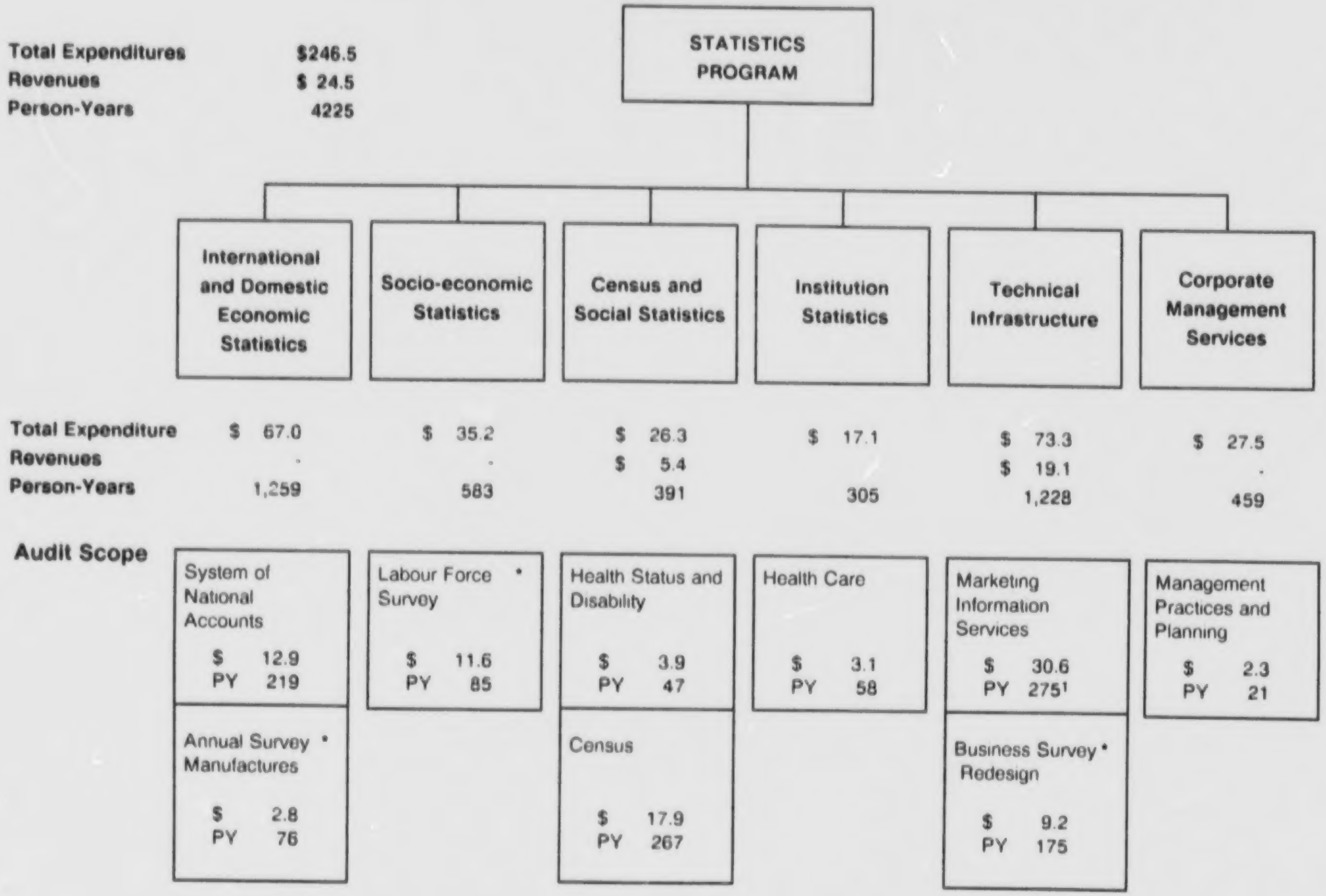
20.10 Statistics Canada is a highly professional organization with over 900 professional and scientific staff. It provides data to meet a very broad range of requirements. To determine the specific types of data that are required, the Agency supplements its own professional expertise with communication links it has established with stakeholders in governments, business and labour unions, the academic community and the media. It faces a practically limitless demand for more and better data. Statistics Canada recognizes that meeting all users' needs is virtually impossible.

20.11 Since our last comprehensive audit in 1983, the Agency has put in place a National Statistics Council and a network of advisory committees for specific activities. The Council and the advisory committees provide advice on program priorities and relevance. The Chief Statistician has placed a priority on human resource management. Statistics Canada has been recognized for its innovative Corporate Assignments Program, designed to provide staff with a wide range of experiences in the Agency. Some additional initiatives include improved in-house training, an annual awards program, and a no-lay-off policy despite significant reductions in person-years.

20.12 The Agency's expenditures, excluding the census, have remained relatively unchanged during the last six years. In terms of 1988 dollars, they were $226.7 million in 1982-83 and $228.6 million in 1988-89 (Exhibit 20.2). During the same period, it made an 11 percent reduction in its person-years from 4,740 in 1982-83 to 4,225 in 1988-89. A

Exhibit 20.1

PROGRAM STRUCTURE, BUDGET, AND AUDIT SCOPE 1988-89
(millions of dollars)


Total Expenditures $246.5
Revenues $ 24.5
Person-Years 4225
STATISTICS PROGRAM
International and Domestic Economic Statistics
Socio-economic Statistics
Census and Social Statistics
Institution Statistics
Technical Infrastructure
Corporate Management Services
Total Expenditure
Revenues
Person-Years
$ 67.0
-
1,259
$ 35.2
-
583
$ 26.3
$ 5.4
391
$ 17.1
305
$ 73.3
$ 19.1
1,228
$ 27.5
-
459
Audit Scope
System of National Accounts
$ 12.9
PY 219
Annual Survey Manufactures *
$ 2.8
PY 76
Labour Force Survey *
$ 11.6
PY 85
Health Status and Disability
$ 3.9
PY 47
Census
$ 17.9
PY 267
Health Care
$ 3.1
PY 58
Marketing Information Services
$ 30.6
PY 275¹
Business Survey Redesign *
$ 9.2
PY 175
Management Practices and Planning
$ 2.3
PY 21

*Source: Part III of the Estimates 1988-89 Forecasts; * from Statistics Canada*

1 *Does not include 240 py's dedicated to cost recovery work.*

further reduction to 4,103 person-years is planned for 1989-90. Thus, during this period, the Agency has been required to reduce person-years and operate on a budget that has not grown in real terms, with an increased proportion of the funds coming from revenue-generating activities.

20.13 At the same time, it has been attempting to meet the demands for new data and improvements in existing data, maintain its position of professional leadership and continue to contribute to innovations in statistics. The Agency has put a great deal of effort into improving its productivity through increased automation and integration of production activities. Initiatives have also been taken to increase vote-netted revenue from $12.7 million in 1982-83 to $24.5 million in 1988-89 (in constant 1988 dollars).

20.14 In order to provide funds to carry out the 1986 Census of Population, Statistics Canada reduced its net expenditures by approximately $68 million. It did this through a combination of reducing expenditures and increasing revenues over a five-year period. At the time of our audit, the Agency was faced with the management challenge of coping with continuing resource constraint.

Observations

20.15 There is a recognition within government that Statistics Canada needs to maintain its independence in statistical matters in order to carry out its mandate in an unbiased manner. Although commonly referred to as an agency of government, Statistics Canada is formally a government department, currently reporting to the Minister of Regional Industrial Expansion. The reporting and accountability requirements are those of a government department, not a Crown corporation.

There is a recognition within government that Statistics Canada needs to maintain its independence in statistical matters in order to carry out its mandate in an unbiased manner.

20.16 All government managers are expected to account for the responsibilities they are given and are answerable for their actions and stewardship. Because of its accepted independence in statistical matters, there is an even greater obligation on the part of Statistics Canada to report to Parliament, through its Minister, on program choices that have been made and the effect of those choices on the statistical products concerned. Statistics Canada has an additional obligation to the users of its products to provide full and complete information on the quality of those products, any changes that may have been made to them and the consequences of the changes on their main uses.

20.17 It is in the nature of an audit report to emphasize negative findings, and this chapter is no exception. As outlined in the audit scope, we did not examine all of the Agency's activities. While we report here on areas for improvement, we observed a widely held respect by many data users for the Agency's professionalism. In our examination, we noted a dedication on the part of Agency staff to maintaining good statistical practice. We also found that most managers satisfactorily carried out their statistical activities in conformity with the Agency's guidelines for maintaining quality. Because of the nature of our reporting, these examples have not been included.

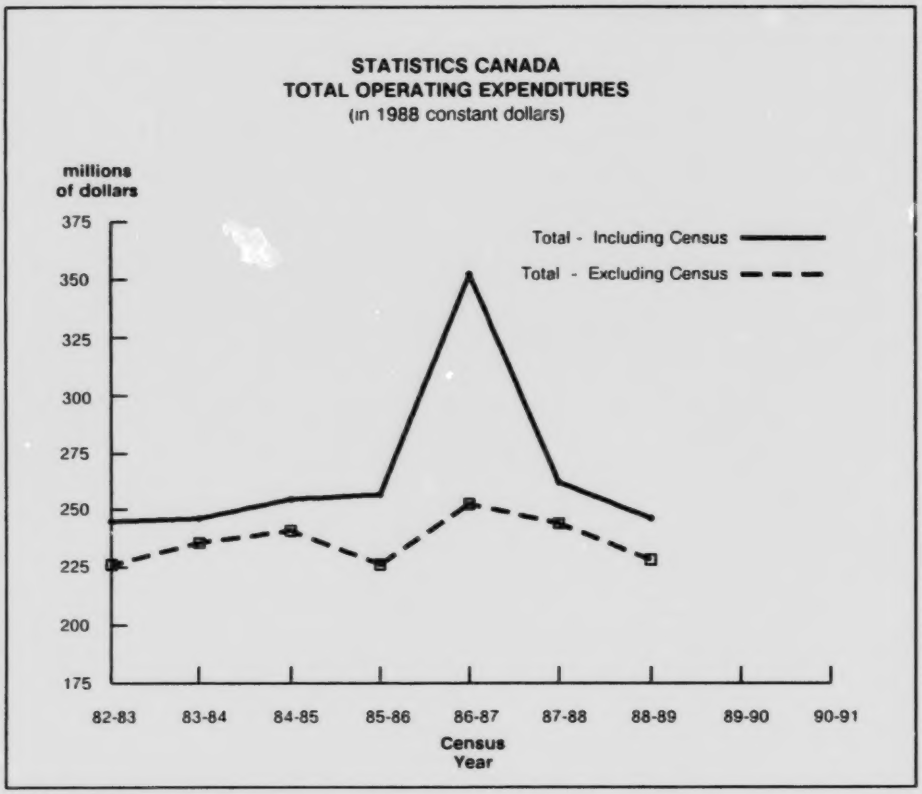


Exhibit 20.2

Planning

20.18 Since our 1983 audit a formal planning process has been established in the Agency. In 1987 the overall planning priorities and directions for the Agency were outlined in the Strategic Overview. The current planning process is built on the input of program managers, which is consolidated for review by more senior levels of management. Each level of management meets and discusses the long-term planning proposals, which include proposals for meeting efficiency targets and contingency plans for coping with further reductions. Managers bring to the planning meetings a wide range of inputs, as described in paragraphs 20.8, 20.10 and 20.11, as well as the results from federal-provincial consultations, internal analysis of social and economic issues and program evaluation.

20.19 A key task in statistical management is the setting of priorities, since there will always be competing demands for, and limits on, resources. Effective allocation of the Agency's increasingly scarce resources rests on making appropriate choices from among a multiplicity of user demands and pressures for increasingly timely and reliable statistics within the context of its mandate.

20.20 The Strategic Overview states that the planning process is based on the assumption that the current program mix can only be changed at the margins. The outcome of this planning approach is that many new needs have a lower priority, in the short term, than existing programs.

Increased automation has reduced the number of person-years required to prepare statistical outputs (see paragraph 20.13).

20.21 The Chief Statistician has identified a number of serious data gaps. Cost savings have been made through program reductions that limit the amount of data collected, the frequency with which they are collected or the size of samples. The Agency intends to fund new initiatives judged to have the highest priority primarily through these marginal reductions and through savings that result from increased efficiencies.

20.22 The current planning process deals with large program areas which it does not formally link to the operational plans of specific surveys or data gathering activities. For example, because of the level of aggregation in corporate planning documents, the Labour Force Survey and the Annual Survey of Manufactures cannot be identified except where they are offered as possible areas for savings. Program profiles used in an Agency-wide review did not provide enough detail to make these two surveys identifiable.

20.23 In a statistical agency, choices about the priority to be given to a particular data series are based on assessments of the costs involved and of the type and precision of data required to meet legislative requirements and the needs of the main users. However, in our examination we found that information with the statements of activity objectives in the planning process did not consistently specify the type and precision of data required to satisfy the main users and the legislative requirements. As a result the process could not consistently provide accountability statements of the effects of the marginal changes in response to budget reductions in terms of activity objectives.

20.24 In 1983 we reported that, in planning or managing data series, management did not appear to be making explicit, wherever possible, the required level of reliability of data which could be related to their main uses. The Agency stated that it agreed with the underlying intent of our recommendation that these requirements should be made explicit. However, it favoured a less "mechanistic" approach because it had no objective basis for assessing the relative importance of the various uses. It also argued that technically it was not possible to measure many of the factors affecting reliability.

20.25 Other central statistical agencies have established processes that deal with the problem of specifying the type and precision of data requirements to meet the needs of main users and legislative requirements. Explicit statements of data requirements for data series are made for planning and accountability purposes. These statements are not always quantified but are as specific as is technically possible.

20.26 In the continuing development of its planning processes, Statistics Canada should provide more specific information with the statement of activity objectives of the data required to meet the needs of the main users.

Management's response: *In addition to the long-term planning process, a variety of mechanisms are used to keep the total program of the agency under regular review: Ministerial directives; systematic monitoring of Cabinet memoranda; consultations with ministerially appointed National Statistics Council; formal interdepartmental committees; an active internal analytic program; a variety of federal-provincial mechanisms; formal program evaluations undertaken through contract by leading external experts; some 15 professional advisory committees; client contacts with thousands of users; market feedback through sales; contacts with trade associations, Chambers of Commerce; networking with academia; and international consultations with a view to facilitate international comparisons by our clients.*

Formal documentation of main users and uses is maintained at the subactivity level. Extending this to some 415 distinct statistical activities would involve unproductive additional paperwork.

1986 Census of Population

20.27 Every five years a census of population is carried out in Canada. The census every tenth year, at the beginning of the decade, is required by the constitution; it provides the basis for determining representation in the House of Commons. The mid-decade census is constitutionally required for only two of the western provinces, but it is required by the Statistics Act for all of Canada. In 1956 the mid-decade census became a national census.

20.28 Statistics Canada prepares options and recommendations on the content of the census. Cabinet makes the final decisions on its content, and on the size of the expenditure, based on this advice.

20.29 Traditionally the census at the beginning of the decade has been larger than the mid-decade census. In both cases, questions are included to provide basic population counts and personal information about the total population. Questions are also included to obtain additional information from a sample of the population -- 20 percent in 1986. These questions, in both the 1981 and 1986 censuses, give cross-classified data for small geographic areas, providing information on detailed relationships, for example, between occupation, industry, income and education. According to Statistics Canada, these data on small sub-provincial areas are unavailable from any other source.

20.30 A census of population is a major undertaking. All Canadian adults are involved. For the 1986 Census about 42,000 people carried out the enumeration and other field activities at a total cost of approximately $150 million. The projected budget for the 1991 Census including estimates for population growth and inflation, is $265 million, depending on the number and types of questions that are recommended to, and approved by, Cabinet.

20.31 Published population figures are required for payment of funds under a number of federal acts and regulations. Under the Federal-Provincial Fiscal Arrangements and Established Programs Financing Act, the Chief Statistician is required to provide a certificate stating the population counted in each province in each census year and an estimate of the population in the years between.

The requirement to reduce census costs

20.32 Census planning typically starts as soon as data collection for the previous census has been completed. Statistics Canada began a review in 1982 of federal government requirements for 1986 Census data. There were bilateral consultations with federal and provincial government users, as well as with other census data users such as municipalities, businesses and universities. In November 1984, the government announced that the 1986 Census of Population, as planned, would be cancelled to generate savings of $100 million in the period 1985-86 to 1987-88.

20.33 On 21 December 1984, the Minister announced the reinstatement of the 1986 Census, since Statistics Canada had developed an alternative plan to realize the $100 million savings. The savings, according to the Minister's announcement, were to be achieved by the following methods:

- reducing the data gathered, resulting in a smaller census operation;
- increasing the emphasis on cost recovery. Users of census and other data would be expected to bear a fairer share of the costs;
- establishing the 1986 Census as a Federal Government Student-Youth Employment Program; and
- phasing out some programs, unless cost recovery was realized. Some programs would be expected to take a place behind the census.

Risks associated with the change in the census were not identified

20.34 In his announcement reinstating the census, the Minister expressed confidence in the ability of Statistics Canada to sustain a high level of statistical quality. The Chief Statistician advised Treasury Board that the commitments associated with the reinstatement of the census posed rigorous challenges, but these would be met without damaging the technical infrastructure of the Agency or its statistical programs. Compared to the usual four-year planning period for a census, Statistics Canada was required to make sudden cost-cutting changes in only five months. In the planning of the "revised" census, we saw

Approximately 42,000 people were employed in carrying out the 1986 Census of Population (see paragraph 20.30).

no documentation of analysis of the risks associated with certain of the choices that had to be made to achieve savings.

Savings were achieved through operational changes in the census-taking

20.35 In addition to using summer students instead of traditional census representatives, all paid advertising and postal checks were eliminated. There were also substantial reductions in telephone assistance services available to census respondents. Many of the operational procedures that were changed in this fashion had been developed originally to ensure maximum inclusion of the population in past censuses.

Little reduction from the 1981 census in the amount of data gathered

20.36 One of the ways, suggested by the Minister, of achieving the $100 million savings was a reduction in the amount of data gathered, which would result in a smaller census operation. We were advised by Agency officials that there was a small reduction in the size of the originally approved census questionnaire. Two questions were eliminated, and the level of detail in a third was reduced. The size of the mid-decade census in 1986, however, required a significantly larger number of responses to questions than the previous mid-decade census in 1976. The 1986 Census was only 4 percent smaller in terms of the amount of data gathered than the 1981 decennial Census.

Reductions limited the benefits from one census question

20.37 One of the cost savings introduced, for example, was a change in processing the answers to the question about address of place of work (question 28). The incremental cost of collecting the data was estimated in 1983, at the planning stage, to be $2.2 million; approximately $1.5 million of this would be for coding the responses. To save the cost of coding, it was decided that the information from the question would only be provided to municipalities that paid for the coding. As a result, this information has only been coded for the province of Ontario, which paid for the coding of the responses. The responses from the rest of Canada for this question remain uncoded.

The quality of the population count was reduced

20.38 The changes in operational procedures had a significant negative impact on the quality of the population count. Statistics Canada has developed a statistical technique, "the reverse record check", to estimate the size of the "undercount" -- that is, the number of people not included in the census count. For 1986, the undercount was estimated to be 3.21 percent which was 60 percent higher than in 1981. This means that an estimated 839,000 people were not included in the population count. The estimate of the undercount in 1986 is the highest recorded since undercoverage was first measured in 1966. The Agency, in its review of past census operations, considered the 1981 census an "unprecedented success" in terms of factors such as the operations, cost, timeliness and completeness of the population count. In that census an estimated 2.01 percent of the population was not included in the count.

20.39 Population size, as certified by the Chief Statistician, is used to determine the payments to provinces and territories from the federal government for established program financing (health, post-secondary education) and for equalization. These annual transfers in 1988-89 were approximately $25 billion. Relatively small changes in population figures can have a significant impact on the amounts of funds that are transferred. Although a completely accurate census is an unattainable goal, a number of procedures have been established to minimize the error in the census count and the likelihood that a reported change in population is the result of errors in measurement.

20.40 The Chief Statistician considers it professionally indefensible to link a dollar value to the undercount because, in his view, no adequate methodology has been developed in Canada to estimate the size of possible double-counting (overcount). The Chief Statistician notes that the statistical profession, both in Canada and the United States, is deeply divided about the reliability of these estimates. Statistics Canada has made no estimate of the net error in the census count. In the United States, estimates of net undercount are made. Officials in Canada have expressed the opinion that the size of the underestimate is larger than the size of the overestimate.

20.41 While some error in population count is inevitable, maintaining a consistently high quality is important to ensure fair and equitable distribution in the main federal transfer programs. Population figures from one census influence the determination of the payments over a six-year period. Changes in figures can result in significant changes in the payments.

20.42 Statistics Canada should continue to investigate ways and means of developing a basis for estimating net census error.

Management's response: *The agency for many years has investigated, developed and implemented improvements in methods used to measure the quality of census data, including measures of coverage. An explicit program to continue this research in conjunction with the 1991 Census has been in place since 1987.*

Users need more information on the impact of the change in undercount

20.43 The Chief Statistician is responsible for furnishing statistics to users and providing advice on their quality. In general, census results are provided to users through the Agency's standard dissemination channels. The Chief Statistician is also required to provide certification of the population numbers for specific programs as part of their legislation. None of the certificates that were based on the 1986 Census includes any reference to the quality of the data.

20.44 In July 1988, the Agency issued a user information bulletin that reported the undercoverage rates of the 1986 and 1981 censuses by province. None of the catalogued publications on the 1986 Census we reviewed, however, that provided population numbers, referred to the increase in the undercount numbers since 1981. Consistent with Agency guidelines, users of census data need to be provided with this information in census publications.

20.45 Users of census data should be provided with more information about the size of changes in the undercount in both publications and certifications.

Management's response: *Consistent with its policy of informing data users about the quality of its statistical products, the agency will continue to provide census data users with information about coverage errors, including the estimated undercount. Output plans for the 1991 Census will be reviewed to determine whether additional information can usefully be incorporated in publications and other forms of output. It must be noted, however, that information on the estimated census undercount is not available until after the main census results are published.*

Unspecified effects on other agency programs

20.46 Half of Statistics Canada's targeted savings of $100 million were made by 1986-87, primarily from savings in census operations. The remainder was to be recovered over the next three years. This commitment has placed a financial burden on Statistics Canada. Savings targets, even with further financial restraint, have been met. The impact on other programs attributable to the required savings for the census is difficult to determine, as described in paragraphs 20.51 to 20.59 and 20.80 to 20.82. However, we believe that Statistics Canada has an obligation to advise Parliament whenever significant program reductions and other changes are made, such as those that are associated with going ahead with the 1986 Census.

The alternative of a smaller mid-decade census

20.47 The Statistics Act requires that a mid-decade census be taken; however, the amount of information that should be included in the census has not been legislated. Statistics Canada has estimated that 70 percent of the cost in 1981 and 78 percent of the cost in 1986, was explicitly required by statute. Over time, censuses have been used to collect an expanded range of data beyond the base requirement. From 1976 to 1986, the mid-decade census changed from a smaller census to almost a complete replication of the full decade census, including a larger number of discretionary questions than previous mid-decade censuses.

20.48 Census taking is a complex and expensive undertaking. All of the discretionary items in a census can also be collected in other household surveys for smaller numbers of people. The increasing size of the mid-decade census has been justified by Statistics Canada because of its uniqueness as a source of small-area detailed data and demands for the data by users. Statistics Canada argued that this change was warranted because of changing data requirements and the need for nationally available small area data and because the required information was not available from any other source.

20.49 Changes are continually being made in the development of new data sources. Alternatives to meeting the discretionary portions of the census may be available from the development of new data sources to respond to priority needs. Examples of such sources would be the selective use of other sample surveys and projections built on the updated sampling frame from the census.

20.50 Statistics Canada should continue its examination of options for meeting the discretionary mid-decade data requirements in the most cost effective manner.

Management's response: *The agency continuously seeks to meet information requirements of users in the most cost-effective manner. Such an examination was carried out prior to the 1986 Census, and another is already under way for 1996.*

System of National Accounts

20.51 The System of National Accounts provides an integrated system of information on Canada's economic activities, both domestic and international. It produces well known economic measures and tables, including gross domestic product, gross national product, balance of international payments, financial flows, input-output tables, price indices and productivity measures. The forecast expenditure for National Accounts in 1988-89 was $12.86 million and 219 person-years.

Need to define the risks associated with delaying research and development on the system of national accounts

20.52 In a 1980 review of Agency methodology, Sir Claus Moser observed that research and development are essential to maintaining high statistical standards. For a statistical office, these functions provide the basis for adapting to changing technological and institutional situations. There have been a number of major changes in the economic environment in Canada, including a shift toward service industries and the increasing use of technology. If it is to reliably reflect the changing economy, the System of National Accounts needs to reflect these changes.

20.53 The statistics from the National Accounts play an important role in the development and analysis of economic policy. There is therefore an ongoing concern about the quality of the data in the accounts and the relevance of the accounts to current economic conditions. Statistics Canada has done several reviews and evaluations to assess the System of National Accounts and to identify the type of development work that needs to be done to ensure that the overall credibility and relevance of the system is maintained.

20.54 This research and development work is recognized by the Agency as important. However, although an additional pool of staff was provided to improve the accounts, many of them were used to meet more pressing operational requirements. For example, more than half had been assigned to work on the implementation of the harmonized system and the Business Survey Redesign Project.

20.55 An assessment should be made, for internal planning purposes, of the risks associated with delaying research and development in the identified areas in the National Accounts.

Management's response: *The consequence of not doing this work has been recognized and acted upon. In recent years research and development topics included: total factor productivity; satellite accounts for tourism and health; the underground economy; personal savings; chain price indexes; and expanded measures of industry output by province and* *deflation of the main components of final expenditures in the provincial accounts. Particular attention has been paid to improving coverage of services activity, both within Canada and in trade with other countries. This has entailed a re-examination of concepts and definitions, as well as development of new surveys and publications. During the recent historical revision, new price indexes were introduced to reflect the rapid growth of computing capacity. Additional work is, of course, underway.*

Need to improve documentation on national accounts for the users

20.56 As we pointed out in 1983, it is essential that users be provided with enough information on the quality of the data in the National Accounts to allow them to determine the data's appropriateness for their specific purposes. The National Accounts are derived from complex data sources and there is a necessary arbitrariness in some of the steps used in constructing the accounts, including imputations and adjustments of data.

20.57 Users require complete and up to date information on the data and methods used in the System of National Accounts. Documentation of sources and methods is frequently postponed under pressure to meet deadlines. More published information on data sources and methodology employed in the System of National Accounts is needed by users.

More publishing information on data sources and methodology employed in the System of National Accounts is needed by users.

20.58 Furthermore, the Business Survey Redesign Project will change the way many of the economic series that make up the National Accounts are collected. In December 1988, the new sampling frame was used for the monthly Wholesale and Retail Trade Surveys. In our 1983 audit we noted that problems with the sample frame at that time resulted in an underestimation of the value of retail trade for input into the National Accounts. To compensate for this, upward adjustments to the results were made. The new frame is designed to improve the estimates from the survey. However, these changes will in turn affect the data in the accounts and potentially the use and interpretation of them by users. The Chief Statistician describes the transition period as a time when "the data will likely be more volatile". Users will require more information about the changes in data going into the accounts and how these may affect the results in the accounts.

20.59 The Agency should provide users with more published information on the process of National Accounts construction and the quality of its output.

Management's response: *A large quantity of information is already readily available for interested users. Additional material is currently in preparation or has been recently released. This includes:*

- *A User Guide to the Canadian System of National Accounts; to be released October 1989.*
- *A Guide to the Financial Flows and National Balance Sheet Accounts; published February 1989.*
- *A methodology document for monthly estimates of GDP by industry; first draft to be available by the Spring of 1990.*
- *A methodology document for service producing industries in the Input-Output Accounts; completed November 1987; a similar document for goods producing industries; in preparation. Publication scheduled for 1990.*

- *A new sources and methods publication for National Income and Expenditure Accounts as series of separate handbooks covering major components; to be released periodically over the next two years.*

Labour Force Survey

20.60 The Labour Force Survey produces the official monthly estimates of unemployment and characteristics of the labour force. The survey is based on a complex sample design covering 48,000 households. The data are usually released 13 days after the last questionnaires have been completed, or about 3 weeks after the questionnaires are sent into the field. In 1988-89 the survey cost $11.6 million and used 85 person-years and 800 part-time interviewers. Some of the main users of the survey are the Canada Employment and Immigration Commission and other federal and provincial government departments.

No clear statement of survey objectives defining data requirements

20.61 As part of the overall requirement to reduce expenditures, the sample sizes of some surveys, such as the Labour Force Survey, were reduced. The statement of survey objectives is not supported by a specification of the level of reliability needed by the main users of the data. As a result, Statistics Canada could not state the effects of these reductions on the data, in terms of the survey's objectives.

20.62 In 1986, 5,217 households were dropped from the survey as part of the general budget cut in Statistics Canada. This change has affected the precision of some of the statistical estimates. Users were informed of these changes in precision. Contingency plans for further reductions in sample size that would have resulted in the provision of only national and provincial data were developed during the planning process. These plans were not implemented.

20.63 Statistics Canada is defined as the provider of data under the Unemployment Insurance Act. There is no statement of what statistical data are required under the Act. The findings from the Labour Force Survey are used to estimate unemployment rates by unemployment insurance economic regions. These rates, in turn, are used in criteria for determining eligibility for, and durations of, certain benefits. A difference of one percentage point is used to determine entrance requirements and half a percentage point the weeks of benefits. Reductions in sample size increase the likelihood that this difference will come about as a result of sampling variability rather than a real difference.

Annual Survey of Manufactures

20.64 The Annual Survey of Manufactures dates back to 1917. In 1987-88, it cost over $2.8 million and used 76 person-years. The outputs of the survey are an integral part of the wider economic statistics program, including the System of National Accounts.

20.65 The data collected by the survey provides information on the manufacturing sector of the economy. This sector accounts for more than one-fifth of Canada's real domestic product, roughly 17 percent of total employment, and some 65 percent of the nation's total exports of goods and services. The data can also be used in the analysis of the changes arising out of trade liberalization, including the effects of the Canada-United States Free Trade Agreement. The two major sets of data produced are principal statistics providing operating data such as financial and employment figures and detailed commodity statistics of Canadian manufacturing industries.

No clear statement of survey objectives defining data requirements

20.66 As part of the overall requirement to reduce expenditures, greater reliance has been placed on estimation than on direct surveying. As in the other surveys examined, there was no statement of the data requirements of the main users of the Survey of Manufactures as part of the objectives. As a result, Statistics Canada could not state the effects of the changes in this survey, in terms of the survey's objectives.

Increased use of estimation

20.67 Several changes have taken place in the survey since 1983. In 1987 the name of the survey was changed from a census to a survey of manufactures, in recognition of the increased reliance on sample surveys to collect data from smaller manufacturing establishments. The level of resources assigned to it has been reduced. There has been a shift from long- to short-form questionnaires, with greater use of taxation data and increased use of estimation procedures. The long-form questionnaire covered about 93 percent of manufacturing shipments in 1986. For manufactures not covered by the long-form questionnaire, there is a reduction in the detailed commodity statistics collected, and estimates are provided instead. The use of the sampling frame produced by the Business Survey Redesign Project will produce further changes.

Lack of timeliness of publications

20.68 The Agency recognized that publications releasing the results of this survey were not timely; in 1984, the publications were reviewed to improve timeliness. There was some improvement in the release of the principal statistics for 1985, but further slippage for 1986. The main timeliness problems, however, are with the commodity statistics. For the reference year ending in 1985 (including the 31 March 1986 year-end), the first commodity publication was released in January 1988.

20.69 Commodity statistics for 1987 were not edited because of a lack of resources. There were 36 people working on editing the 1986 data; only 15 were available to do this work for the 1987 data. As a result, the 1987 data will not be published. The frequency of publication of the commodity statistics is being reviewed.

Health Statistics

20.70 Health statistics refer to series on vital statistics, information about health care institutions and their use, disease registries, and surveys related to health status, knowledge and attitudes. The forecast budget for health statistics in 1988-89 was $5.8 million and 94 person-years.

20.71 Health care and its costs are an issue of increasing national concern. In 1987, the total cost of health care in Canada was nearly $47.8 billion, shared by all levels of government and individuals.

Need to ensure the ongoing cost-effectiveness of Statistics Canada gathering data on hospital operations

20.72 In its Strategic Overview, Statistics Canada defines improvement in information on the health of individuals as one of its program priorities. The Chief Statistician has personally taken a lead role in several initiatives designed to bring about substantial improvements in health information. Several of the statistical series related to health care institutions have been collected by the Health Division for several decades. In our review of the data collected by the Health Division, we found there was little evidence of a continuing need for Statistics Canada to provide some of these health care institutional data. Examples of activities with uncertain importance for Statistics Canada are described below.

Data on hospital operations

20.73 Information about the operation of hospitals is a major effort of the Health Division ($200,000 non-salary expenses and 20 person-years in 1987-88). The bulk of operational data is still being collected and published as it was in 1976-77. The two main data bases produce the following detailed information:

The Quarterly Hospital Information System is largely a data base used for making comparisons among hospitals. There are approximately 435 indicators per hospital, including type of service provided, ownership, selected diagnostic and treatment services, number of meal-days, kilograms of laundry, etc. In 1986 the Advisory Committee on Health Statistics recommended that this system be put on a cost-recovery basis. The Committee recommended that, if hospitals and provinces did not purchase the data, the program should be discontinued; the recommendation was not accepted. A federal-provincial working group on hospital information, at Statistics Canada's request, considered the need for Statistics Canada to collect these data. They raised questions about the need for Statistics Canada to continue to collect them but did ask that the system be maintained.

Annual hospital statistics. Data from provincial ministries make up the annual hospital statistics data base. This contains information similar to the quarterly data but in more detail. The Advisory Committee on Health Statistics questioned the need for this degree of detail. The data are produced with considerable delays -- publication is expected two years after the end of the reference period. The Canadian Hospital Association has developed a new hospital management information system that will standardize the input from all provinces. With common reporting across the provinces, comparisons can be made directly. This raises further questions about the need for Statistics Canada's involvement.

Morbidity data

20.74 These data are obtained from institutional records at a cost to the division of $227,000 (non-salary expenses) and eight person-years. Annual statistics on hospital admissions and separations are provided by the provincial ministries. The Hospital Medical Records Institute is developing a similar data base for management information. It is now processing about 75 percent of the admissions/separations from Canadian hospitals. Statistics Canada processes 100 percent of the data for statistical purposes but doesn't produce it as quickly as the Hospital Medical Records Institute. This raises the question of the continuing need for Statistics Canada to allocate scarce resources to this area.

20.75 Statistics Canada should reassess the ongoing requirement to provide hospital-based statistics.

Management's response: *Disagree, given the fact that the federal-provincial working group on hospital information concluded that the data continue to be needed. Moreover, the recommendation as presented places inadequate weight on the comprehensive initiatives currently under way to improve the entire program of health statistics. Statistics Canada has assumed a leadership role in the reassessment of the existing program of health statistics. A new National Health Information Council, reporting to the Chief Statistician and the Conference of Deputy Ministers of Health, provides a forum for reviewing the requirements for health information of all kinds, whether derived from* *hospital or other administrative files, population-based surveys or other sources. Statistics Canada is also collaborating with the Canadian Institute for Advanced Research with the objective of developing a new paradigm for health information to help guide future statistical and analytic work.*

Business Survey Redesign Project

20.76 The Business Survey Redesign Project is one of the largest and most complex projects Statistics Canada has undertaken. The major planned output is a more complete and up-to-date business register to which all redesigned business surveys will be linked. The project has important implications for a variety of operational activities, including the Annual Survey of Manufactures and the System of National Accounts. It also responds to some of the observations made in our 1983 Report.

20.77 At its peak in 1987-88, the project involved direct expenditures of $9.2 million and 175 person-years. Cumulative expenditures from 1984-85 to the end of October 1988 have been $27.2 million. It is not yet complete; actual testing of the new register had just begun at the time of our examination.

Need to state the implications of resource allocation to a major new project in a period of restraint

20.78 Statistics Canada undertook the Business Survey Redesign Project at considerable internal cost. It justified the priority placed on the project by the need to improve the current business surveys, reduce the response burden on businesses and provide more complete coverage of economic activity. In the spring of 1984 Treasury Board approved approximately 45 additional person-years for each year of the three-year planned duration of the project. Although it was recognized at that time that internal reallocations would have to provide the major part of the necessary funding, the negative implications of these reallocations for other activities were not documented in plans and proposals.

20.79 Overly ambitious targets were set for the project. At the time of our audit, it was running about a year and a half behind the original plans. Deadlines continued to slip during 1988. Project delays have resulted in additional pressure on resources and delays in documentation for other surveys such as the Annual Survey of Manufactures. Project milestones were set out in Part III of the Estimates but the failure to meet them has not been consistently reported.

Data Dissemination

20.80 The Statistics Act requires Statistics Canada to make public the information it collects. The data gathered by Statistics Canada are made available in a variety of forms, including printed publications, electronic data bases, and other electronically readable data products. The Agency also operates public information and inquiry services and a communications program. New Agency policies on data dissemination, a requirement to increase cost recovery, and overall budgetary constraint have changed the level of service being provided to the public by Statistics Canada.

There is a need to define clearly the difficulty in meeting established levels of service as a result of changing demand and budgetary constraints

20.81 The Agency guarantees public access to its general information. A recently developed Agency marketing policy makes the commitment to free access to information through a variety of dissemination mechanisms. These include a toll-free telephone inquiry service, regional reference centres and the provision of complimentary publications to provincial and territorial governments and the media. Also included is the Depository Services Program of the Department of Supply and Services, which provides complimentary publications to selected libraries and to federal Members of Parliament.

20.82 The Agency carries out ongoing reviews of service quality. These reviews, and our own audit work, show that resources have not kept pace with significant increases in the demand for some services. As a result, there has been a lowering of the level of service. For example, more telephone inquiries by users go unanswered in Toronto, Montreal, Vancouver and Ottawa offices. And the consolidation of publications has resulted in less free data going into the Depository Services Program.

Publishing

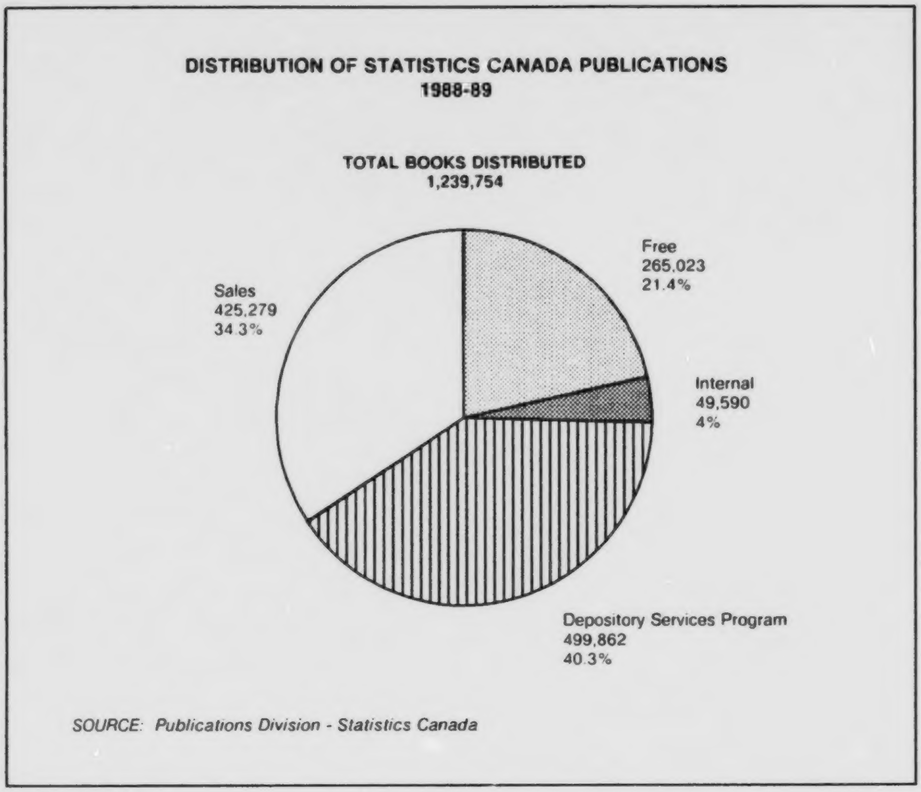
20.83 Our 1983 audit noted that "most directors choose to disseminate information through printed publications". Our current audit concluded that publication is still the most common means of dissemination. This year Statistics Canada will produce more than 450 titles covering a broad range of statistical information. Over 1.2 million copies of publications were distributed in 1988-89. Twenty-one percent of these were distributed free through library exchange programs, distribution for provincial statistical focal points, and the media. Four percent were distributed internally. Forty percent were distributed through the Depository Services Program. Supply and Services Canada pays incremental costs to Statistics Canada for this distribution through the Depository Services Program. Treasury Board has temporarily increased estimate reference levels in order to make up for shortfalls in revenue from this program. The remaining 34 percent of publications are sold (see Exhibit 20.3).

Lack of proper authority to set prices and sell publications

20.84 The Statistics Act does not give the Agency specific legislative authority to set the selling prices of its publications. Before 1984, the Department of Supply and Services had this responsibility. In 1984 a memorandum of understanding was signed confirming and describing publishing responsibilities between Statistics Canada and Supply and Services. Statistics Canada was given all publishing responsibility for "fully priced" and "supported price" general publications, responsibility to maintain and manage inventories, as well as the right to retain publications sales revenue. Upon signing the memorandum, Statistics Canada took on its new responsibilities and also set its own publication prices.

20.85 Treasury Board approved the arrangement in the memorandum of understanding for a two-year period. At the end of the two years, an evaluation by the two departments was required before the arrangement could be made final. Although the evaluation was never undertaken, the agreement was extended by the Deputy Ministers of Supply and Services and Statistics Canada. Treasury Board has not been formally advised of this arrangement and has not given its approval. Without Treasury Board approval for the extension of the memorandum of understanding, Statistics Canada is setting prices and selling publications without proper Board authority.

20.86 The arrangement for assuming responsibility for publications set out in the memorandum of understanding between Statistics Canada and the Department of Supply and Services should be evaluated by the two departments as required by the Treasury Board, and resubmitted to the Board.



SOURCE: *Publications Division - Statistics Canada*

Exhibit 20.3

Management's response: *Statistics Canada has been discussing with the Treasury Board Secretariat for some months an articulation of the role the agency should have in the management of its publications. These arrangements will be formalized.*

Absence of required approvals of current prices

20.87 The Department of Supply and Services obtains Treasury Board approval of its approach to publication prices. It does this by obtaining approval of a costing model and pricing system for all its publications. All Government of Canada publications that are published and distributed by the Publishing Centre are priced using the costing model. The Publishing Centre normally sets prices based on the costs. There is also a provision to adjust prices to a "market value" if it is higher than the cost.

20.88 Statistics Canada has not obtained approval of its pricing structure for publications; its policy is to recover the cost to the government. We reviewed Statistics Canada's publication pricing practices. Its current prices are not based on a costing model and pricing system similar to the Publishing Centre. We found that the procedure for setting prices included additional factors beyond those included in the Publishing Centre approach.

20.89 Statistics Canada should obtain appropriate approval for the pricing system for its publications.

Management's response: *When Statistics Canada obtained full delegation for publishing its own publications, it sought guidance from the Department of Justice and was advised that it had the power to set prices for its publications under the agreement.*

Publications information system does not provide adequate cost information

20.90 There have been delays in implementing management information systems to meet the needs of the Publications Division. Information is currently not available in the system to estimate the full cost of publications sold.

21

DEPARTMENT OF SUPPLY AND SERVICES

21

DEPARTMENT OF SUPPLY AND SERVICES

Main Points

Scope of the review

21.1 The objectives of this year's review were twofold. The first was to follow up and assess the adequacy of corrective action undertaken by the Department of Supply and Services (DSS) in response to our 1987 audit of its government-wide administrative services. The second was to determine client departments' perceptions of the cost and quality of DSS government contracting services by conducting an opinion survey (paragraphs 21.18 to 21.20).

Follow-up of our 1987 audit findings

21.2 DSS management has commenced corrective action, most of which is still in progress. Some of the more significant productivity issues reported in our 1987 chapter will take time and effort to resolve. Systems and infrastructures that were designed to suit the 1970s technology are gradually being transformed to fit the needs of the 1990s (21.21 to 21.51).

Opinion survey of government contracting services

21.3 In general, client departments are satisfied with the central role played by DSS in the government contracting process. However, concerns were expressed over the timeliness of awarding contracts, delivery, and the cost and quality of goods and services procured. DSS clients suggested improvements in the process of planning and administration of the government contracting process (21.52 to 21.100).

Department's conclusion

21.4 The reflections in this chapter convey an understanding of what is happening within the Department and provide an objective and professional point of view. The information included in the chapter will be of value to the continuing process of effecting change in the Department.

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DEPARTMENT OF SUPPLY AND SERVICES

Introduction

21.5 The Department of Supply and Services (DSS) was formed in 1969 as part of a general administrative reorganization of government in response to a concern for efficiency and economy in government operations.

21.6 Its mandate derives from the Department of Supply and Services Act, the Financial Administration Act, the Defence Production Act, and numerous Orders in Council and Treasury Board Administrative Policies. In addition, DSS has several Memoranda of Understanding which govern its relationships with other departments and agencies.

21.7 Within government, DSS is known as a common service organization providing goods and services to virtually all federal departments and agencies. These goods and services are delivered within a framework of policies established by the Treasury Board and with sensitivity to the broader objectives of government such as regional or industrial development.

21.8 According to Treasury Board policies, the primary role of common service organizations is the provision of service to their client departments and agencies, and, within that role, the primary goal is the attainment of maximum value for money. In addition to Treasury Board policy and procedures, many of the activities of DSS are directed or constrained by other authorities such as the Minister of Finance or the governing legislation and policies of individual departments and agencies DSS serves. Therefore, DSS activities are conducted in a complex environment where the objectives of service, control and value for money may conflict.

21.9 To deliver its various service lines, the Department employs close to 9,500 people and is organized into six major areas (see Exhibit 21.1).

21.10 The Supply Operations Sector is responsible for the acquisition of and contracting for goods and certain services on behalf of other government departments and agencies and co-managing major crown projects. All contracting services are provided to clients on a fee for service basis.

21.11 The Management and Operational Services Sector is responsible for the overall management and functional direction of government-wide administrative services such as accounting, computing, and other related services provided to government departments and agencies.

21.12 The Regional Operations directorates are the vehicle for day-to-day delivery of the Department's common services through a national network of District Supply and Services Offices.

21.13 The Finance and Administration Sector provides corporate financial and administrative support to the Department.

21.14 The Corporate Policy and Planning Sector provides planning, program direction, policy formulation and review, internal audit and program evaluation for the Department.

21.15 The other corporate functions include the Department's legal, human resource and public affairs services.

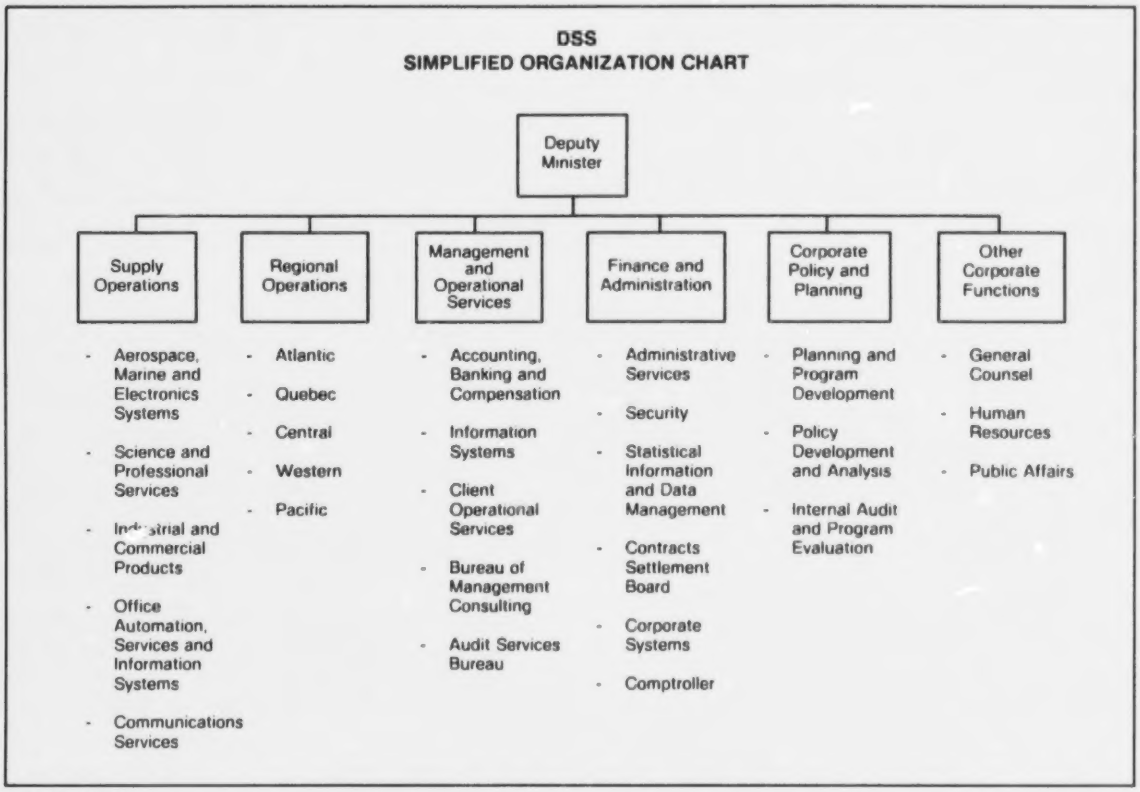
DSS
SIMPLIFIED ORGANIZATION CHART
Deputy Minister
Supply Operations
Regional Operations
Management and Operational Services
Finance and Administration
Corporate Policy and Planning
Other Corporate Functions
- Aerospace, Marine and Electronics Systems
- Science and Professional Services
- Industrial and Commercial Products
- Office Automation, Services and Information Systems
- Communications Services
- Atlantic
- Quebec
- Central
- Western
- Pacific
- Accounting, Banking and Compensation
- Information Systems
- Client Operational Services
- Bureau of Management Consulting
- Audit Services Bureau
- Administrative Services
- Security
- Statistical Information and Data Management
- Contracts Settlement Board
- Corporate Systems
- Comptroller
- Planning and Program Development
- Policy Development and Analysis
- Internal Audit and Program Evaluation
- General Counsel
- Human Resources
- Public Affairs

Exhibit 21.1

Scope of the Review

21.16 In our 1987 audit of DSS, we reported on our evaluation of the management controls over the delivery and the productivity of government-wide administrative services provided by the Management and Operational Services Sector.

21.17 In our 1988 audit we reported on the procedures used by DSS to ensure that suppliers of goods and services, contracted for by the Supply Operations Sector on behalf of other government departments, complied with the terms and conditions of government contracts. We considered key contract conditions, particularly those pertaining to departmental contract audits.

21.18 The objectives of this year's review were twofold. The first was to follow up and assess the adequacy of corrective action undertaken by the Department in response to the recommendations in our 1987 annual report.

21.19 The second objective was to determine client departments' perceptions of the cost and quality of DSS contracting services by conducting an opinion survey.

21.20 The first part of this chapter deals with the follow-up of our 1987 audit. Results of the opinion survey are contained in the second part of the chapter.

Follow-up of our 1987 Audit Findings

Background

21.21 The government-wide administrative services provided by DSS and reported on in our 1987 audit report included Public Service Pay, Public Service Superannuation, government cheque issue and related support functions. Our audit was particularly concerned with the ability of DSS to deliver services of acceptable quality at a reasonable cost.

21.22 We concluded that, while the Department had maintained adequate service quality, its service costs were high, its delivery systems were labour intensive and it had not fully exploited the benefits available from automation. We recognized in our 1987 chapter that corrective action to address these issues represented a major challenge for DSS management and indicated that, to improve productivity, the Department should:

- set cost and quality targets for all products or service lines and develop the necessary strategic plans for their achievement;
- establish clear and responsive accountability relationships for the cost and performance of each service line under the new plans;
- ensure that appropriate human resource skills are put to use in developing and implementing these plans;
- develop automated systems capable of achieving planned service line cost and quality targets; and
- develop adequate management information tools in the areas of cost accounting and performance measurement to control and monitor the performance of each product or service line.

21.23 Our follow-up review assessed the adequacy of corrective action taken by the Department in response to the 1987 chapter. The initiatives of the Department in responding to our recommendations are set out below.

Corrective Action

21.24 **Strategic planning.** The Department is currently undertaking an extensive strategic planning exercise intended to evaluate its service lines to reach a common understanding with its clients and central agencies as to future courses of action to be taken. Several Service Line Studies, which are completed or currently underway, are designed to evaluate the Department's current activities, its role and the cost-effectiveness of alternative modes of service line delivery and performance measurement options.

21.25 **Service lines' costs.** The cost and quality of service lines delivered by a common service organization, such as DSS, should be major criteria in assessing its overall performance. DSS service lines' costs should compare favourably with those of similar organizations.

21.26 In our 1987 audit we selected the DSS Public Service Compensation services, as a sample of DSS service lines, for comparison with other organizations. Our analysis indicated that the DSS compensation service costs were significantly higher than those of the organizations we reviewed.

21.27 DSS is currently undertaking a major project to reduce its compensation service line costs by developing a new, integrated Public Service Compensation System. This system is intended to increase the use of automation and take greater advantage of modern technology.

The objectives of this year's review were twofold. The first was to follow up and assess the adequacy of corrective action undertaken by the Department in response to our 1987 audit of its government-wide administrative services. The second was to determine client departments' perceptions of the cost and quality of DSS government contracting services by conducting an opinion survey.

21.28 In June 1989 Treasury Board approved $11.5 million for DSS to complete the feasibility study for this project. The Department estimates the total cost of the project to be $55 million, including costs to other departments. Once fully implemented in 1995, potential savings within DSS for Public Service Compensation services are estimated by the Department to be up to $23 million annually. Upon the completion of the feasibility study, DSS will be in a position to refine its estimates of the total costs and the potential annual savings of this project.

21.29 Since our 1987 audit, DSS has introduced automation into the calculation of retroactive Public Service Pay changes and the issue of urgent government cheques. There has also been a gradual increase in the use of the Public Service Pay on-line data capture system by DSS clients. DSS is planning to further increase the use of this on-line data capture system. This would result in further operating cost reductions at DSS.

21.30 DSS annually prints and mails approximately 110 million cheques to the public for socio-economic payments such as Canada Pension Plan, Old Age Security and Family Allowance. DSS has recently obtained government approval to deposit these cheques directly into the banks of the recipients who wish to receive direct deposits. Savings resulting from the application of this method of payment are estimated by DSS to amount to $7 million annually. This estimate is based on the assumption that 40 percent of the recipients would accept the direct bank deposit method of payment. If more recipients accept the new method, the estimated savings would be even greater.

21.31 **Regional operations.** DSS delivers its services through a regional network of District Supply and Services Offices. The productivity of these operating units is important to the Department's overall cost effectiveness. Comparative information on their productivity is a basic tool for management in identifying potential opportunities for efficiency improvements and is a prerequisite to corrective action.

21.32 In 1987 we analyzed the productivity of certain parts of these operating units, which employ approximately 2,700 people, and determined that there were long-term opportunities for the Department to improve productivity in this area of its operations, particularly in the small offices. We also reported that DSS did not have the management tools to measure and report on the productivity of its regional operations.

21.33 Since 1987, DSS has eliminated the position of Assistant Deputy Minister, Regional Operations and reduced its regional staff by 120 person-years from the 1987 levels.

21.34 Further productivity and efficiency gains in regional operations should result from the following initiatives which were described above:

- implementation of the newly designed Public Service Compensation System;

- increase in the use of the on-line data capture system; and
- increase in the use of direct bank deposit of government cheques.

21.35 DSS management indicated that internal studies, which are currently underway, are examining ways of rationalizing the regional operations and assessing their future role.

21.36 The Department has recently implemented a new performance measurement system for its regional operations. Periodic reports are now being made available to DSS management on a limited distribution basis. The new system measures a region's performance against a base period in addition to its performance relative to other regions.

21.37 In conjunction with its Service Line Studies, DSS is performing a post-implementation review of this new system. It is still too early to evaluate the degree of its usefulness for management in monitoring the performance of regional operations.

21.38 **Development of technology.** In 1987 we encouraged the Department's project, which was in process, to rationalize its five multi-technology data centres across Canada and consolidate them into a single technology data centre. We recognized that this rationalization was a prerequisite for DSS to develop new, modern systems and to improve human resource skills.

21.39 The project was recently completed. Reductions of approximately 65 person-years in DSS have resulted from the rationalization of technology even though the workload handled by DSS's newly equipped data centre has significantly increased over the same time period.

21.40 DSS management indicated that it is examining ways to introduce more automated technology into its newly consolidated data centre operations to rationalize workloads and achieve further operating cost savings.

21.41 The results of our review of the Efficiency of Federal Government Data Centres, including those of DSS, are scheduled for reporting in next year's report.

21.42 **Development of computer systems.** Management controls over planning and conducting systems development projects are needed to ensure that the cost of automation development is minimized and that the potential benefits of automation are realized and reflected in lower service line costs.

21.43 In 1987 we reviewed DSS management controls over selected major systems development projects. The results of our review indicated that the computer systems development experience at DSS had not been consistently successful. The Department has now adopted a new systems development methodology which sets out guidelines for project management. The focus of the methodology is on deliverables or outputs at specific points throughout the term of the project.

21.44 Overall, we found that the policies, guidelines and standards needed to address the concerns expressed in our 1987 chapter regarding systems development were in place. However, formal procedures to support their use were still in development, or had been implemented too recently to allow for a realistic evaluation of their effectiveness.

21.45 **Cost information.** Sound productivity management depends on reliable, timely and useful information, including that produced by performance measurement and cost accounting systems.

21.46 The 1987 audit reported that DSS did not have full cost information on its products or service lines.

21.47 DSS has now developed a costing system which is designed to capture and report full service lines costs and to provide the necessary data to support cost comparisons. However, it is not yet widely used by DSS product managers and therefore it is too early to evaluate the degree of its usefulness for management in monitoring and controlling costs of services.

21.48 A common service organization such as DSS should provide members of Parliament with information that would allow them to evaluate whether the services provided by the Department are delivered in a cost-effective manner.

21.49 In our 1987 chapter we reported that the information in the Part III Estimates and the Operational Plan Framework, which were centred around the organization structure, did not provide a clear picture of the nature and costs of service lines offered by DSS.

21.50 No significant changes have yet been made but the Department plans to provide Part III Estimates on a service line basis after the completion of its Service Line Studies. This approach is not expected to be finalized before 1991 due to the extensive co-ordination required.

Conclusion

21.51 DSS management has commenced corrective action, most of which is still in progress. Some of the more significant productivity issues reported in our 1987 chapter will take time and effort to resolve. Systems and infrastructures that were designed to suit the 1970s technology are gradually being transformed to fit the needs of the 1990s.

Opinion Survey of Government Contracting Services

Background

21.52 In 1987-88 the Supply Operations Sector of DSS issued some $10 billion worth of contracts for goods and services on behalf of other government departments and agencies (see Exhibit 21.2).

21.53 In a common service organization such as DSS, the level of client satisfaction with the quality and cost of the contracting service it provides to its customers is a significant indicator of the Department's performance.

21.54 To obtain the perceptions of DSS clients, we conducted an opinion survey of certain client departments, accounting for approximately 50 percent of the volume and value of contracts issued by DSS, about the quality and cost of the contracting services provided to them.

21.55 We interviewed approximately 140 senior officials and operational personnel in the selected departments, who were representative of the client departments in the area of materiel management and operations. We sought their general perceptions concerning DSS contracting services, based on their extensive experience with such services.

21.56 To ensure that these general perceptions were reasonable, we selected a sample of contracts and interviewed the client department operational personnel who had initiated them, concerning their experiences with the specific contracts selected in our sample. The results of these interviews, and comments received from client officials, are reported in the following sections of this chapter.

VALUE OF CONTRACTS ISSUED BY DSS ON BEHALF OF OTHER GOVERNMENT DEPARTMENTS AND AGENCIES

(Fiscal Year 1987-88)

Customer Department	Billions of Dollars
National Defence	$ 6.1
Canadian Commercial Corporation	1.0
Transport	0.4
Regional Industrial Expansion	0.2
Canadian International Development Agency	0.2
Environment	0.2
Fisheries and Oceans	0.2
Energy, Mines and Resources	0.2
Royal Canadian Mounted Police	0.1
National Research Council	0.1
Agriculture Canada	0.1
Correctional Services	0.1
Employment and Immigration	0.1
Public Works	0.1
Health and Welfare	0.1
Other clients	1.2
	$10.4

Exhibit 21.2

21.57 To select our sample we obtained a listing of contracts issued by DSS with a value of $100,000 or more. We excluded major crown projects (over $100 million) because each is unique.

21.58 From this listing we selected a random base sample of contracts for each department included in the review. From the base sample we judgmentally selected 143 completed contracts for the interviews. We attempted to include, in our selection, contracts covering the range of goods and services that are essential for the main mission and operations of the selected client departments.

21.59 Our opinion survey of client department officials covered the following areas:

- DSS participation in the contracting process;
- timeliness of contract award and delivery of goods or services;
- achievement of quality requirements;
- costs of goods or services,
- user fees charged by DSS;
- client departments' direct buying authority; and

- Government policy objectives.

21.60 The following are the survey findings on client perceptions and suggestions for improvement. They are reported for further evaluation by DSS in conjunction with its internal studies currently underway.

Opinion Survey Findings

DSS participation in the contracting process

21.61 All contracts issued by DSS require the co-operation and joint effort of both DSS and the requisitioning client department to achieve a successful conclusion. The degree of DSS participation varies from stage to stage in the process.

21.62 Client department operational personnel reported medium to high levels of participation by DSS in developing sourcing strategies, issuing requests for proposals, evaluating proposals, issuing contract documents, and negotiating contract terms and conditions. Few respondents reported that DSS participated in developing specifications for, or inspecting the quality of, the goods and services contracted through DSS (see Exhibit 21.3). Respondents were generally satisfied with the DSS contract officers' knowledge of products and markets and with the level of their communication with them.

21.63 However, there was a consensus among DSS clients that, after contracts are awarded, the role of DSS in administering them is limited. Although respondents reported a certain degree of DSS participation in contract administration, it was described as involving only the processing of paper, legal documents and payment claims. Most clients reported that DSS was not generally involved in the ongoing monitoring of the progress of contracts, but would participate, on an exception basis, if the client reported a problem.

21.64 Although DSS has the mandate to ensure the quality of goods and services procured, it has delegated most of this responsibility to the client departments through mutual agreements or practices established over the years.

21.65 Client department officials suggested that:

> DSS should play a more active role in the area of contract administration relating to monitoring suppliers' compliance with quality requirements, delivery dates, performance milestones and other significant terms and conditions of a contract.

Timeliness of contract award

21.66 Timeliness of awarding contracts for goods and services is important to the efficiency of government operations.

21.67 In our opinion survey, 3 percent of the client department operational personnel could not address this issue. Those who could reported that 22 percent of the selected contracts were not awarded in a timely fashion while 78 percent were. The elapsed time required to issue the selected contracts, as compared to the time perceived by clients to be reasonable, varied, depending on the size of the contract. The perception of client department officials was that most delays occurred in either the very large or the very small contracts. Many respondents reported that most delays occurred during the stages of issuing requests for proposals or bids and during contract negotiation (See Exhibit 21.4).

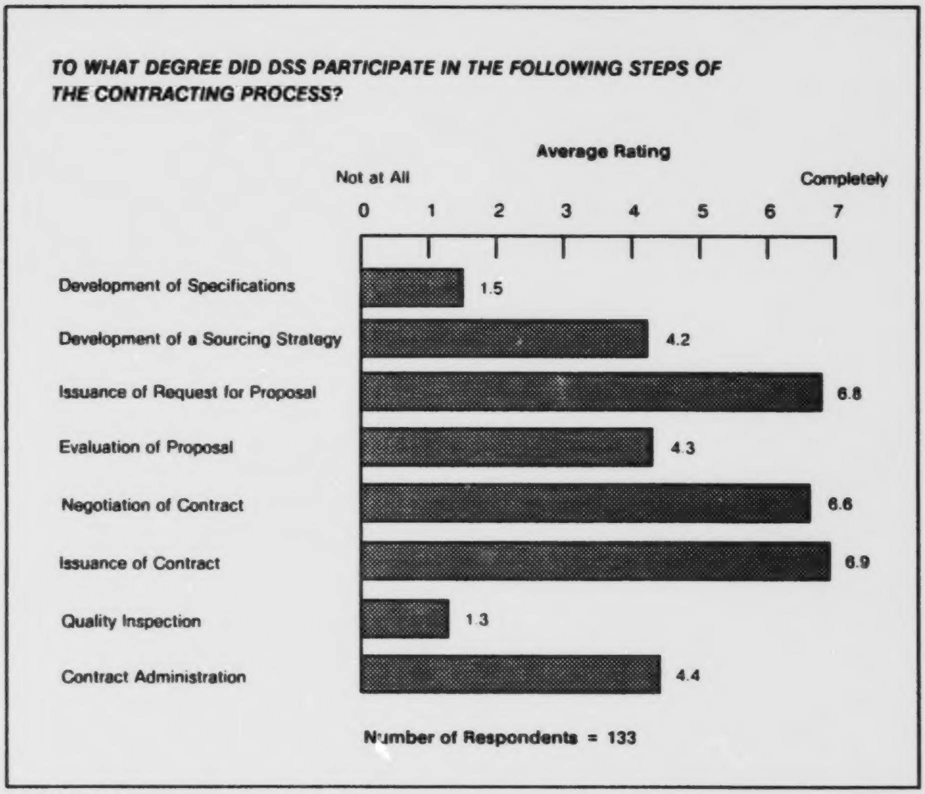

Exhibit 21.3

21.68 Some of the other delays were reported as occurring in developing specifications and in raising and transmitting requisitions to DSS. Such steps in the contracting process take place within the client departments and are, therefore, not the responsibility of DSS.

21.69 Respondents often commented that delays in awarding contracts occur due to excessive workloads of DSS contracting officers and that more streamlining of the contracting process at DSS and in client departments is required.

21.70 To improve the timeliness of the contract award process, client department officials suggested the following:

- Increasing the client departments' level of authority to directly handle and issue small contracts would reduce the volume of low-value contracts issued by DSS and result in reduced clogging of the DSS system.
- Increasing the use of standing offer arrangements, whereby DSS would pre-negotiate and pre-approve a contract with a specified supplier, would permit client departments to place their orders directly with that supplier without having to go through DSS each time goods or services are ordered.
- Client departments should ensure that their specifications for goods and services are current and accurate, to avoid delays caused by DSS returning them for adjustment.

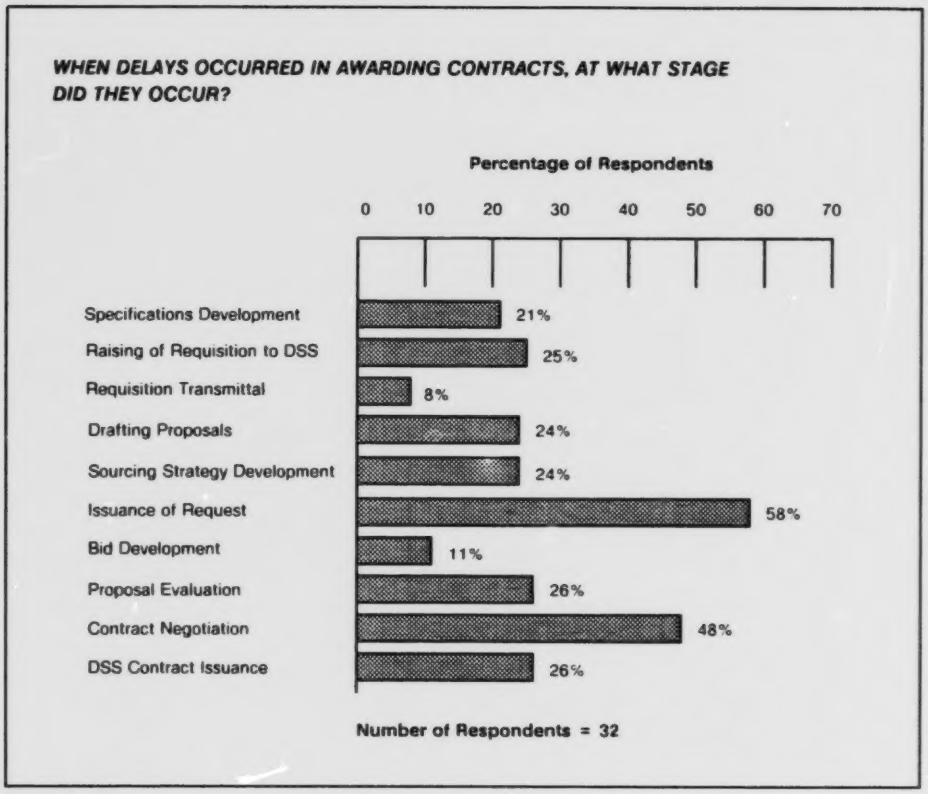
WHEN DELAYS OCCURRED IN AWARDING CONTRACTS, AT WHAT STAGE DID THEY OCCUR?

Exhibit 21.4

- Lists of suppliers should be refined to ensure that only fully qualified suppliers are invited to respond to requests for proposals. By eliminating unqualified suppliers from DSS's source lists, proposal evaluation time could be reduced.

- Contracts that are routine and simple should have a system which is simpler than that required for the complex ones. The use of telex and telephone orders for such contracts should be encouraged.

- There should be an increase in the use of modern technology in the contracting process to reduce paper work and improve timeliness.

21.71 Several respondents felt that improved communication between the client departments and DSS would facilitate the timely issuance of contracts. Early communication by client departments to DSS about planned requirements and contracting needs was viewed as important. A few respondents suggested situating a DSS contract officer in client departments would facilitate communication.

Timeliness of delivery of goods and services

21.72 Delays in the delivery of goods and services may affect departmental operations and program performance, and could result in budgetary problems.

21.73 In our opinion survey, 3 percent of client operational personnel could not answer questions related to this issue. Of those who could, 23 percent reported that timeliness in the delivery of goods and services was a problem. In 77 percent of the selected contracts, delivery was reported to have been timely.

21.74 Of the contracts with delays in delivery, most frequently it was the suppliers who were reported to be responsible. Over half the respondents reported that the supplier was almost completely responsible for the delay. Respondents also indicated that both DSS and client departments share some of the responsibility for these delays (see Exhibit 21.5).

21.75 To improve the timeliness of delivery of goods and services, client department officials suggested the following:

- Improve the front end evaluation of suppliers' capabilities, to ensure that prime contractors and sub-contractors can provide the required goods or services on time.
- Remove delinquent contractors from the DSS list of suppliers.
- Improve monitoring of supplier performance and enforce contract terms for progress and delivery.
- Encourage and enforce the use of penalty clauses and liquidated damages in government contracts.
- Negotiate a more realistic time frame for the delivery of goods and services.

Achievement of quality requirements

21.76 Client departments determine their need for goods and services and establish their statements of requirements and specifications. When the goods and services are received, they are inspected by client department officials to ensure that the requested specifications have been met. Failure to achieve contracted quality requirements may result in delays in operations, impact on safety, and result in extra cost to the government or the supplier.

21.77 In our opinion survey, 8 percent of client department operational personnel could not address this issue. For those who could, it was reported that in 96 percent of the sample contracts selected the goods and services met or almost met departmental quality requirements. However, concerns about quality were reported in 4 percent of the contracts in our sample. The concerns were reported in contracts for services as well as in contracts for goods. We noted that quality problems tend to occur in the contracts which have a high degree of technical complexity.

21.78 Quality inspection was seen by respondents as being the responsibility of the clients who set the specifications, determined the quality requirements and inspected the goods or services on delivery.

21.79 In those contracts where quality requirements were not met, client officials indicated that the reasons were most often related to a poor choice of supplier or to problems with the client specifications for the goods or services. In some cases poor choice of supplier was the result of constraints in selecting them. For example, choices having to be made amongst a limited number of suppliers, sometimes as a result of directives related to national and regional industrial, Canadian content, or small business policy objectives. In some of the contracts in which quality was a concern, the client officials reported that the goods and services met the specifications but fell short of the department's requirements. This indicated a failure of the specifications to sufficiently define the department's quality requirements.

WHEN DELAYS OCCURRED IN THE DELIVERY OF GOODS/SERVICES, TO WHAT DEGREE WERE EACH OF THE FOLLOWING RESPONSIBLE?

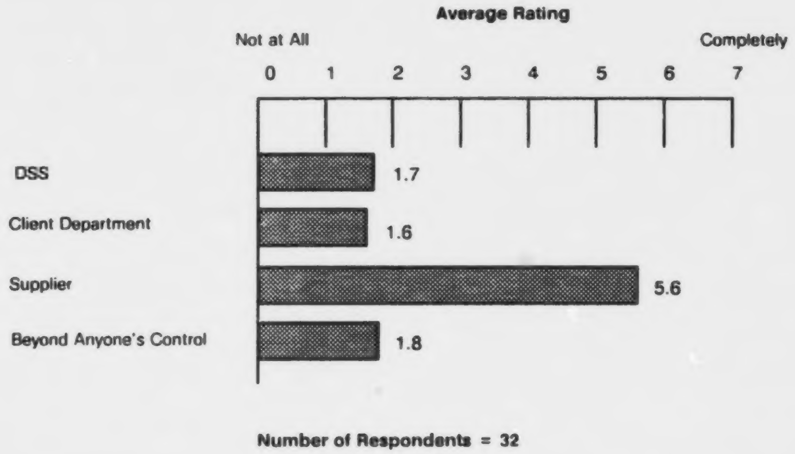

Exhibit 21.5

21.80 Client department officials suggested the following:

- There should be better definition of client quality requirements and improved description of the specifications.
- Improve the front end evaluation of suppliers' capabilities to ensure that they could provide goods or services of the required quality.
- There should be more client involvement in evaluating suppliers' proposals, regardless of contract size.
- Contracts should always be awarded on the basis of best value, which is generally a balance between a fair price, reasonable delivery time and appropriate quality. Lowest price alone should not be the prime factor in awarding contracts.
- DSS should monitor contract performance and ensure that the lists of suppliers are always current, accurate and contain only suppliers with proven track records.

Cost of goods and services

21.81 The value of goods and services contracted by DSS on behalf of the Government of Canada amounted to $10 billion in 1987-88. Therefore, efforts to obtain even a small reduction or discount in the price of these goods and services could result in significant savings. Adequate procurement planning and use of appropriate methods of supply are essential to achieve such savings.

21.82 In our interviews we asked client department officials whether DSS obtained goods and services at the lowest price, apart from those situations in which meeting other government national and socio-economic objectives accounted for a higher price having to be paid. We then asked them whether, had they had complete authority themselves to make purchases directly, they would have been able to obtain the goods and services at a lower price.

21.83 During the interviews, 15 percent of the client operational personnel could not address the first question. Those who could reported that DSS had obtained the lowest price in 95 percent of the contracts selected, while in 5 percent of the contracts, it had not.

21.84 To the second question, 19 percent of the client operational personnel could not respond. Those who could reported that in 4 percent of the contracts selected, DSS had obtained a higher price, in 54 percent an equal price, and in 42 percent a price lower than that which the client departments could have obtained had they had the mandate (see Exhibit 21.6).

21.85 Limited qualified sources of supply, government regulations, and restrictions imposed by the use of procurement as a lever to achieve national and regional socio-economic policy objectives were reported as factors restricting DSS's ability to obtain the goods or services at better prices.

21.86 To obtain better prices for goods and services, client officials suggested the following:

- There should be better planning and aggregation of government requirements for goods and services and more use of buying in bulk. DSS should negotiate with the suppliers on a government-wide basis to get better prices and discounts.

- There should be more use of national standing offers, as opposed to standing offers by department, to obtain better discounts on prices.

- The concept of having a lead department should be used to buy equipment which is needed by several departments. A lead department would set up the specifications and test the quality of the equipment; then DSS would buy in bulk on behalf of several departments.

- Client departments should ensure that their specifications closely match their requirements. They should not over-specify or define more detailed specifications than are normally required.

- More commercially available goods should be bought as long as they meet requirements. Client departments should reduce the tendency to request goods that have special specifications not readily available in the market place.

- The buy Canadian policy should be applied in a fashion that ensures that money goes back into the Canadian economy rather than going to Canadian agents of foreign manufacturers.

- There should be more direct buying from the producers rather than through middlemen.

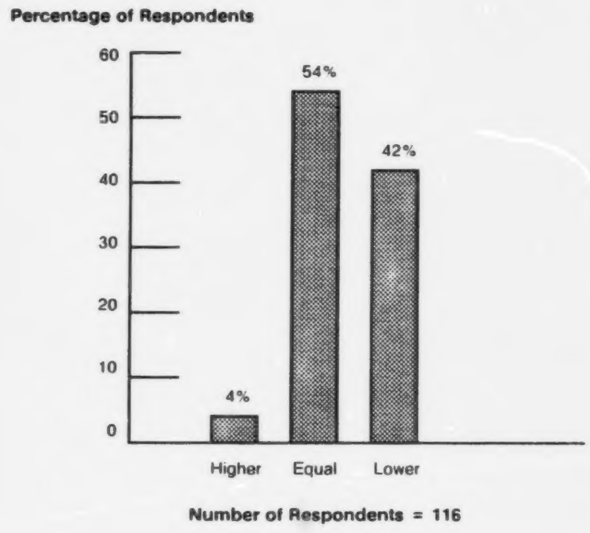
DID DSS OBTAIN A HIGHER, EQUAL OR LOWER PRICE THAN YOU COULD HAVE?

Exhibit 21.6

User fees charged by DSS

21.87 DSS is a revenue dependent department. It recovers from its clients the total cost of its contracting services. The fees charged by DSS are generally based on the dollar value of the contract issued.

21.88 When questioned about user fees, 76 percent of client operational personnel were not aware of the specific fees charged to their departments by DSS for contracting services. Of those who were aware of the fee structure, 60 percent felt that the fees were unfair, 6 percent felt the fees were moderately fair, and 34 percent felt that fees charged were completely fair.

21.89 Many respondents suggested that the fees should be based on the amount of service provided by DSS in awarding and administering the contract, rather than on the dollar value of the contract awarded. Although DSS assigns to each contract a complexity level that reflects the quantity and technical quality of contracting effort required, these complexity levels are not used as factors in setting the fee structure.

21.90 Some officials questioned the appropriateness of charging all of DSS's operating costs to clients, including the cost of the DSS policy unit.

21.91 Other officials questioned why such fees should be recovered at all from client departments.

Client departments' direct buying authority

21.92 DSS policies require that government contracts over $500 for goods and certain services be issued through DSS.

21.93 In our opinion survey, 36 percent of client operational personnel could not express an opinion on whether the level of authority for direct buying by client departments was adequate. However, for those who could, 60 percent felt that the direct buying limit delegated to departments by DSS was too low. Some respondents noted that the dollar value limit had not kept pace with inflation. When asked what the limit should be, 27 percent of those who expressed an opinion felt that it should be raised to $1,000; 38 percent suggested limits of from $1,000 to $5,000, and 35 percent suggested limits over $5,000. Client officials indicated that increasing the dollar value limit of their direct buying authority would reduce the extent to which the DSS system is clogged by contracts of small dollar value.

Government policy objectives

21.94 Government contracting policies require that contracts should be awarded on the basis of best value: the combination of a fair price, reasonable delivery time and appropriate quality, taking into consideration the achievement of national and regional socio-economic objectives of the government. These objectives include national and regional industrial development, Canadian content, and the development of small business in Canada. In addition, government policies require the promotion of competition and the equitable treatment of all suppliers. All government contracts must be awarded on the basis of prudence and probity.

21.95 Our interviews with client officials indicated that they generally perceive the DSS central contracting role as being beneficial to them and contributing to the achievement of the government's national and regional socio-economic objectives; fairness in the selection of suppliers; prudence and probity in contracting; and generally obtaining best value in awarding contracts.

Conclusion

In general, clients are satisfied with the central contracting role played by DSS

21.96 Client departments are generally satisfied with DSS contracting services, and with the assistance provided by DSS contract officers. The DSS central contracting role is viewed as being beneficial to client departments and contributing to the achievement of government national and regional socio-economic objectives, fairness to suppliers and prudence and probity in awarding contracts.

Concerns were expressed over timeliness in awarding contracts, delivery, and the cost and quality of goods and services procured by DSS

21.97 Client officials indicated that some of the factors contributing to these concerns included: inadequate specifications, poor choice of suppliers, restrictions on sources of supply imposed by the use of procurement as a lever to achieve government national and regional socio-economic objectives, the lack of contract penalties and inadequate monitoring of contract performance.

21.98 Respondents suggested the following improvements in the process of planning and administration of the government contracting process:

- Better identification of requirements and specifications with more emphasis on buying goods which are readily available in the market place.
- Careful evaluation of suppliers' capabilities and removal of poor performers from government lists of suppliers.
- Selection of more effective methods of supply, more aggregation of government requirements and more use of national standing offer arrangements.
- Effective enforcement of contract terms, use of penalties in government contracts and effective monitoring of contract performance.
- Reduction of paper work and increase in the use of modern technology in the contracting process.

In general, clients are satisfied with the central contracting role played by DSS. However, concerns were expressed over timeliness in awarding contracts, delivery, and the cost and quality of goods and services procured by DSS

Client officials question the basis of the fees charged to them by DSS

21.99 The fairness of basing the fee structure on the dollar value of the contract was questioned. Many respondents suggested that fees be based instead on the level and complexity of work performed by DSS.

Client departments' direct buying authority is too low

21.100 The current direct buying authority limitation of $500 is viewed as too low. As a result, a large number of small contracts must be awarded through DSS. This increases the DSS workload, and was viewed by some clients as contributing to delays by clogging the system. The majority of respondents suggested increasing the dollar limit of the direct buying authority by client departments.

Department's Response

Follow-up of 1987 Audit

The Auditor General's recognition of DSS's efforts to increase its efficiency and to guide the Department towards improved management of information resources through the application of modern technology is most welcome.

As per our testimony before the Public Accounts Committee regarding the 1987 Report of the Auditor General of Canada, DSS is working towards a state of the art automated operation to better service the federal government, the private sector and the general public while keeping an equilibrium of benefits, pay-backs and the required capital investment.

DSS's commitment to adequately serve our clients in the 1990s within a changing and dynamic environment is encompassed in the Department's reviews of service lines and the related studies, which are currently underway, to further modernize and rationalize our central and regional operations. It is important to note that the pace of implementation of the various technological changes must not exceed our capacity to *absorb the change. The success of this transition, by its nature, is contingent upon an awareness of its logic and impact by all affected users, and the commitment to make it work. We believe that the present culture within the Department and among our client departments is predisposed to such changes. We also wish to stay in step with the private sector players with whom the Department interacts*

Opinion Survey of Government Contracting Services

The survey findings tend to corroborate our own views of client perceptions and our own understanding of the strengths and weaknesses of our acquisition service.

One of the fundamental objectives of DSS is the provision of adequate quality service to our client departments. Our aim, through our service line studies and the modernization of our systems, is to give clients the most efficient and least costly service possible in all areas of Departmental activity.

We acknowledge the need to strengthen our acquisition service in certain areas. Indeed, the chapter provides welcome support to initiatives that the Department intends to pursue, as a result of the current study of our Acquisition Service Line (ASL). One of the objectives of the ASL study is to redeploy professional DSS contracting personnel to higher value-added acquisitions functions, while making greater use of technology for standard commercial transactions. In so doing, DSS will be able to respond more effectively to client service needs, including many of the suggestions that arose during the client survey.

Conclusion

The reflections in this chapter convey an understanding of what is happening within the Department and provide an objective and professional point of view. The information included in the chapter will be of value to the continuing process of effecting change in the Department.

22

DEPARTMENT OF TRANSPORT - CANADIAN COAST GUARD

Protecting Mariners' and the Public's Interest

22

DEPARTMENT OF TRANSPORT - CANADIAN COAST GUARD

Protecting Mariners' and the Public's Interest

Main Points

22.1 Ship Safety. The Coast Guard has allocated the majority of the resources given to the Ship Safety Branch to three areas: performance of mandatory inspections of necessary safety features, development of regulations, and examination of mariners. In these areas its activities appear to be well organized and are carried out by qualified and dedicated inspectors. However, the Coast Guard has not set out specific objectives for its ship safety activities; nor has it done an analysis to identify the areas of greatest relative risk to mariners and to the public interest. The Coast Guard does few random inspections to detect and prevent unsafe operating practices on fishing vessels, unsafe transportation of dangerous goods, or the use of unqualified seamen for critical tasks (paragraphs 22.19 to 22.38).

22.2 Marine Emergencies. At present the Coast Guard has not developed the capability to deal with spills or accidents involving hazardous materials other than petroleum products. The Coast Guard has installed oil pollution containment equipment at various sites throughout the country. Contingency plans are in place for dealing with major oil spills. The Coast Guard has gained some experience in cleaning up various oil spills, but it has not acquired the resources for field responses to major oil spills or spills of hazardous materials other than petroleum products. In responding to a major incident of oil pollution from a ship, the Coast Guard would rely on a joint response network which it has formed. However, the full capability of this network to contain, control and clean up a major oil spill has not been put to the test (22.52 to 22.55).

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Marine Emergencies

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DEPARTMENT OF TRANSPORT - CANADIAN COAST GUARD

Protecting Mariners' and the Public's Interests

Introduction

22.3 The regulatory activities of the Canadian Coast Guard touch the lives of millions of Canadians: when they board a passenger ferry, visit a beach, or make their living in the commercial fishing or shipping industry. Thus, when ferry passengers travel to Prince Edward Island, Newfoundland or Vancouver Island, their safe passage depends, in part, on the Coast Guard's inspections of ships for structural safety, and emergency, fire fighting and navigational equipment.

22.4 The recent spill from the Exxon Valdez on the Alaskan coast has highlighted the risk of the marine environment being fouled by oil. The Coast Guard has the responsibility to contribute to preventing marine emergencies in Canadian waters by monitoring shipments of petroleum products and other dangerous goods.

22.5 This chapter looks at how the Coast Guard plans and operates to meet these challenges.

22.6 The mission of the Coast Guard's Marine Regulatory Program, according to Part III of the Department of Transport's Estimates, has three elements: (1) to develop, promulgate and implement marine regulations and standards to contribute to marine safety and environmental protection; (2) to mitigate the effects of ship-source pollution; and (3) to ensure the provision of workplace safety in the marine industry.

22.7 The program is delivered by two branches of the Coast Guard -- the Ship Safety Branch and the Emergencies Branch, hereafter referred to as Marine Emergencies.

Ship Safety

Background

22.8 In 1989-90, the Ship Safety Branch estimated it would need 412 person-years and $ 25.9 million to carry out its mission. The Branch maintains a central office in Ottawa, regional offices in Vancouver, Toronto, Quebec City, Dartmouth and St. John's, and about 30 district offices.

22.9 The Branch's legal mandate is based on the Canada Shipping Act and other Acts, and on a number of international conventions. Other Acts include the Arctic Waters Pollution Prevention Act, the Safe Container Convention Act and the Transportation of Dangerous Goods Act. The Branch is also responsible for developing and enforcing safety and pollution prevention regulations issued pursuant to those Acts.

22.10 The Canada Shipping Act lays out an inspection and certification regime to ensure that Canadian registered ships contain necessary safety features. The Canada Shipping Act and related regulations cover periodic inspections of a ship and its safety features such as life-saving, fire extinguishing and navigational equipment. These can be referred to as mandatory inspections and, with certain defined exceptions, are applied only to Canadian registered ships -- both new and older ships. Other regulations cover operating practices, such as navigation by qualified personnel, safe handling of equipment on board, use of current charts, etc. The Coast Guard relies to a great extent on the owners and crews of ships to voluntarily follow these regulations.

22.11 In carrying out the mission of the regulatory program, the Ship Safety Branch has established as its primary objectives the development and promulgation of regulations and the conduct of mandatory inspections to promote ship safety. These inspections are carried out by qualified Marine Surveyors who rely on moral suasion and the maintenance of good working relationships with the shipping industry to achieve compliance with the provisions of the Canada Shipping Act dealing with structural safety. The ultimate enforcement sanction is the power of the Steamship Inspector to deny the issuance of an inspection certificate to a non-complying vessel. Daily ship operating costs, in the tens of thousands of dollars, are a powerful inducement for a ship owner to comply with regulatory requirements.

Our examination of ship safety focussed on the planning process used by the Coast Guard to allocate scarce resources for its regulatory activities and its mandatory and discretionary inspections.

22.12 An historical perspective is critical to understanding the Branch's current objectives. A hundred years ago the use of substandard ships in the transportation of timber cargoes and passengers led to numerous accidents and loss of life. The Canada Shipping Act concentrated on safeguarding the ship, the crew and passengers. Protecting the marine environment was given less priority. Since then there have been many changes in both the Canadian economy and the shipping industry--shipping has grown dramatically, "flags of convenience" have become widespread, supertankers are commonplace, and the extensive use of containers is the norm.

22.13 As the maritime environment changes, so do the risks to the public. In our opinion, the Coast Guard now must employ new analytical tools to identify emerging risks to the marine environment; inspection practices that may have been appropriate yesterday may no longer suffice. It must re-evaluate its role and its allocation of scarce resources among its branches which manage various activities such as ship safety, aids to navigation and icebreaking. The challenge for the Coast Guard is to respond to the changing circumstances.

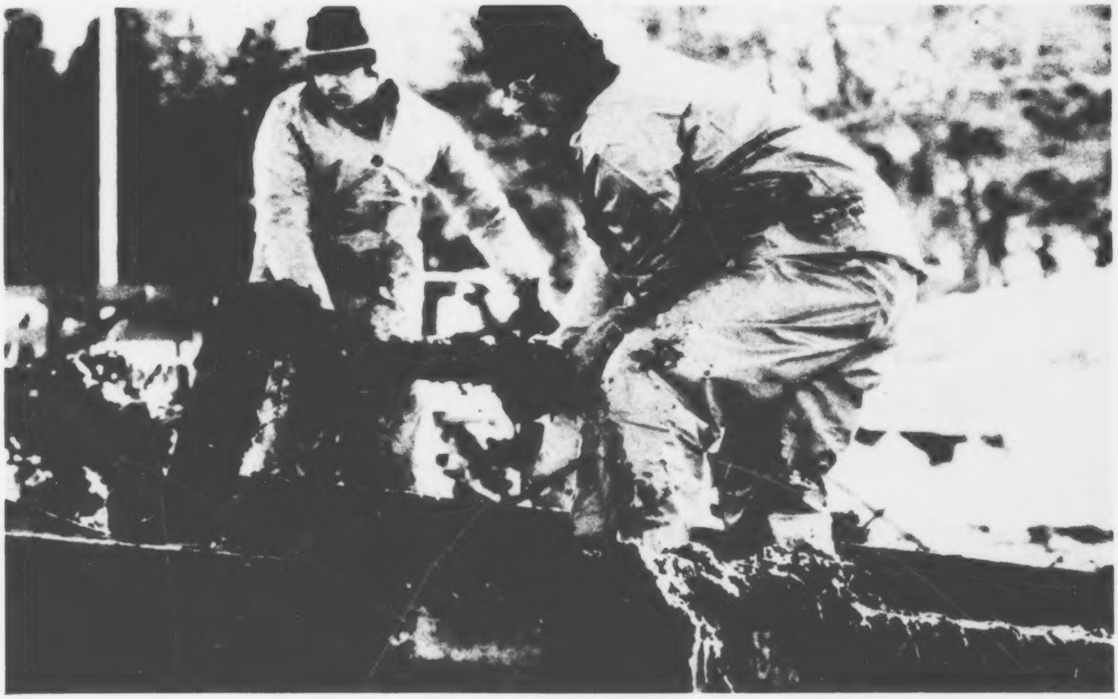
Audit Scope

22.14 Our examination of ship safety focussed on the planning process used by the Coast Guard to allocate scarce resources to its regulatory activities and its mandatory and discretionary inspections.

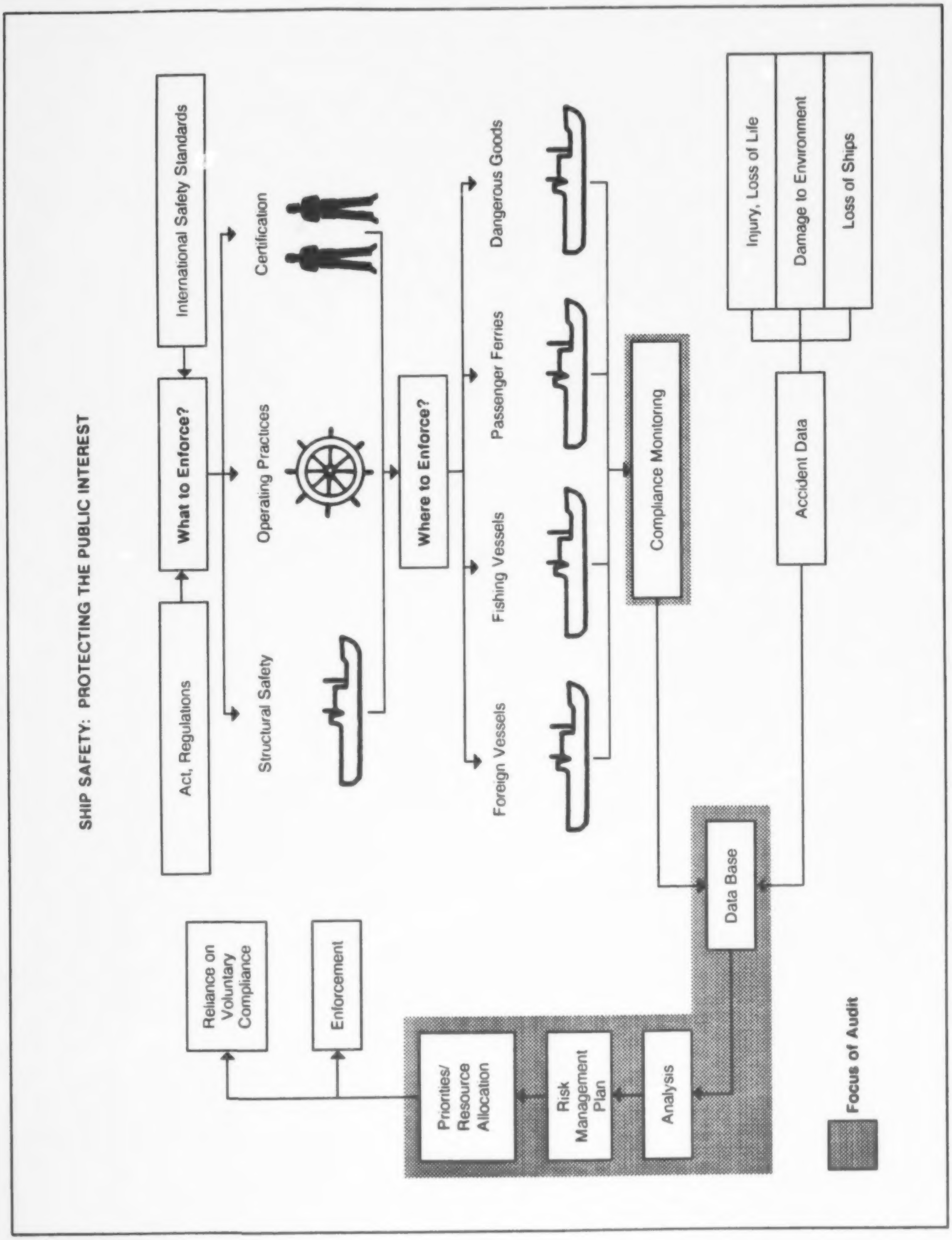
22.15 As illustrated in Exhibit 22.1, "Ship Safety: Protecting the Public Interest", our scope included the data base, the processes for assessment and analysis of risk, and the risk management plans used by the Coast Guard to establish priorities and allocate its resources.

22.16 We looked at systems and activities to promote safety in commercial fishing vessels, foreign vessels, passenger ferries and in the marine transportation of dangerous goods.

22.17 Our audit did not look at the regulation of offshore oil rigs, or examine enforcement of occupational safety.



As the international marine environment changes, so do the risks to the public (see paragraphs 22.12 and 22.13).



SHIP SAFETY: PROTECTING THE PUBLIC INTEREST

Act, Regulations
What to Enforce?
International Safety Standards
Structural Safety
Operating Practices
Certification
Where to Enforce?
Foreign Vessels
Fishing Vessels
Passenger Ferries
Dangerous Goods
Compliance Monitoring
Injury, Loss of Life
Damage to Environment
Loss of Ships
Accident Data
Data Base
Reliance on Voluntary Compliance
Enforcement
Priorities/ Resource Allocation
Risk Management Plan
Analysis
▨ Focus of Audit

Exhibit 22.1

Observations and Recommendations

22.18 Regulatory process. Periodically, the Department implements new regulations and makes revisions to existing regulations. Our comments on the marine regulatory process are covered in a government-wide audit entitled "Special Audits - Federal Regulatory Review Process (Chapter 17)".

22.19 Risk assessment not carried out. The Coast Guard states that almost all regulatory initiatives of the Ship Safety Branch stem from implementation of international convention standards, or from recommendations arising from inquiries into shipping casualties. However, the Coast Guard's Ship Safety Branch has not carried out a formal, comprehensive analysis to determine the best way of promoting safety in marine transportation in the Canadian context. It does not have reliable performance indicators that show what safety results have been achieved and accordingly does not have the information to know whether its current approach will lead to the best results. We recommended in 1983 that the Department develop analytical procedures for monitoring the level of safety in all major areas of risk. The Coast Guard reported that phase one of a risk assessment framework has been conducted. However, our recommendation has not yet been implemented.

22.20 Though a comprehensive assessment had not been done, we found that a risk analysis existed for at least one specific area -- commercial fishing vessels -- that had identified deficiencies and made recommendations for change. In other key areas, such as the operation of foreign vessels and ferries, we found no detailed risk analysis and no regional risk management plans. We noted that the Coast Guard was allocating its resources among the Ship Safety Branch and other programs, such as the aids to navigation program, without the benefit of such a comprehensive risk analysis. We then looked at the allocation of resources within the Ship Safety Branch.

22.21 According to the Coast Guard's records, mandatory inspections, primarily of the machinery, safety equipment and structural safety of a ship, use most of its existing resources -- in some regions, up to 90 percent. This leaves few resources in the Ship Safety Branch for discretionary inspections of safe operating practices. There is no national plan, nor are there national goals, for most types of discretionary inspection.

22.22 Yet there are risks which are not being addressed by mandatory inspections. Our review of the Coast Guard's activities relating to commercial fishing vessels, foreign vessels and passenger ferries identified some of these risks for which the Coast Guard had not prepared regional risk management plans or allocated resources.

22.23 Few inspections of commercial fishing vessels. All of Canada's approximately 41,000 commercial fishing vessels are subject to various safety regulations, depending on their size and operating environment. Only about 4,000 of these fishing vessels are large enough (over 15 gross tons or 24.4 meters in length) to be subject to the requirement for regular safety inspection. Vessels between 15 tons and 150 tons are inspected every four years (about 3,600 vessels), while those over 150 tons are inspected annually (about 400 vessels), as required by the Canada Shipping Act.

22.24 The Coast Guard has stated that improving the safety of commercial fishing vessels is a current priority. In 1987 it conducted a fishing vessel study which reported that from 1982 to 1986, 824 fishing vessels were reported lost, about 90 percent of them smaller than 60 gross tons. One hundred and forty lives were lost over the same period. Of these, 60 percent were on vessels smaller than 15 gross tons -- not covered by the requirement for regular safety inspection. The study also noted that the Ship Safety Branch does relatively little in the fishing fleet to enforce existing regulations. Regulations are enforced only incidentally to a regular inspection or following a reported accident. The majority of fishing

Little monitoring of safe operating practices of commercial fishing vessels (see paragraphs 22.23 and 22.24).

vessel accidents are caused by unsafe operating practices. At the time of our audit the Coast Guard had not developed regional action plans to detect and prevent such practices.

22.25 Foreign vessels not inspected consistently. Up to 80 percent of Canada's offshore trade is carried on by vessels operating under foreign flags. There are at least 12,000 visits by foreign vessels annually at Canadian ports. Except for those carrying grain, timber and ore concentrates, foreign ships are for the most part exempt from the mandatory inspection provisions of the Canada Shipping Act. However, they are required to carry current internationally recognized safety certificates and must declare any safety deficiencies upon entering Canadian waters. Until recently, the Coast Guard rarely ensured that foreign vessels complied with international marine safety standards. But many industrialized nations, including Canada, have recognized the need to verify compliance with these regulations by their use of random safety inspections. In 1987 Canada joined the major European maritime countries in accepting an international agreement, the European Port State Control Agreement, to eventually inspect at least 25 percent of foreign vessels visiting their ports.

22.26 In 1983, we recommended that the Department of Transport review the extent to which foreign vessels comply with Canadian regulations and take action, if necessary, to increase it. Our current examination focussed on the progress made since our last audit and on the present practices for inspection of foreign ships entering Canadian waters. We found that, except for foreign oil tankers, none of the Coast Guard's regional offices had goals for the rate of inspection of foreign vessels. At the time of our audit few foreign ships -- about 7-8 percent -- were being inspected, often after the vessel had steamed extensively in Canadian waters or unloaded its cargo. The inspection rate depended on available human resources rather than on an analysis of risk.

22.27 A high proportion of the inspections that were performed identified serious safety problems -- some serious enough to detain the vessel. For example, in 1988 a foreign ship inspected and detained in Vancouver was found to have lifeboats unfit for use. Duct tape and paint had been used to cover up serious holes and corrosion of the lifeboat shell. In another case, in Halifax, cracks were found in the hull of a vessel and the lifeboats had serious defects.

Foreign vessels entering Canadian waters not inspected consistently (see paragraphs 22.25 to 22.28).

22.28 We noted that a foreign vessel carrying dangerous goods could enter Canadian waters in the Maritimes, not call at any Canadian port, and proceed all the way through the St. Lawrence Seaway into the Great Lakes with little chance of being subjected to an inspection to ensure that it met international ship safety requirements. The Coast Guard does not have an overall plan for meeting the goal of the European Port State Control Agreement to inspect 25 percent of foreign vessels.

22.29 **Safety of passenger ferry operations not emphasized**. Canada is a heavy user of ferries. Annually there are in excess of 20 million passengers on Canadian ferries. Ferries operating in Canadian waters vary in size from small cable ferries to large ocean-going ships on both the east and west coasts.

22.30 Although there have been no major ferry accidents in Canada in recent years, there have been serious incidents in other parts of the world. Recent accidents involving ferries, for instance the sinking of the "Herald of Free Enterprise" in Europe, were caused by unsafe operating practices rather than by unsafe ships.

22.31 We looked at the activities of the Branch in inspecting the ferries operated by the British Columbia Ferry Corporation and by Marine Atlantic. British Columbia Ferry Corporation operated 38 ferries in 1987, carrying more than 18 million passengers and 6.5 million vehicles. Marine Atlantic carried almost 2.5 million passengers and more than 800,000 vehicles in 1987.

22.32 We noted that the Coast Guard had not done an overall risk assessment for passenger ferries, such as would identify key risk areas -- structure, operating practices and the transportation of dangerous goods, for example. An appropriate assessment would also set out the Coast Guard's objectives, jurisdiction and safety priorities. We were informed that the Coast Guard was not aware of the extent of provincial activities or private initiatives in this area.

22.33 For the two ferry operations examined, the Branch had concentrated its activities on the development of extensive regulations and on pre-arranged annual inspections of structural safety, equipment, lifeboats, etc. The Branch had also attended an annual fire drill on every ferry to ensure that the operators were familiar with necessary procedures.

However, the Branch had no formal program of inspecting operating practices. For example, there were almost no random checks of loading and off-loading practices, few checks to ensure that the ferries were under the control of qualified people and few checks to ensure that safety equipment was functional at all times.

22.34 An example of a potentially hazardous situation is the illegal transportation of dangerous goods on passenger ferries. Ferry operators rely on declarations by transporters that dangerous goods are not among those being shipped on passenger ferries. The Ship Safety Branch does not have a program to monitor or inspect such shipments.

22.35 For the most part the Coast Guard relies on others to ensure that safe operating practices are followed. We noted that it had done only limited verification to find out whether this reliance was justified.

22.36 The Coast Guard does not have national or regional risk management plans. Such plans would identify the skills, materials, and other resources required to meet its priorities and would include a multi-year schedule showing time frames and areas covered. It would also highlight any risks not provided for in the action plan. The plan would indicate areas where the Coast Guard relied on others to ensure, for example, the safety of passenger ferries in Canada. The Coast Guard would then be in a position to determine the impact of its activities on such areas as ferry passenger safety, and to identify gaps in its coverage.

22.37 Overall, we concluded that the Coast Guard had not developed analytical procedures for assessing risks related to the safety of ships and had not prepared risk management plans. It allocates its resources based on historical patterns for mandatory inspections rather than on an analysis of current needs.

22.38 The Coast Guard should assess current risks to the safety of ships and prepare national and regional risk management plans that allocate resources relative to risk.

Departmental response: *The Department accepts the recommendation and will continue with ongoing efforts which will contribute to the assignment of resources based on risk management plans.*

Human factors are the leading cause of accidents in small fishing vessels and will be dealt with by improved safety education, certification for masters of smaller vessels and passive protective features in the vessels. Additionally, enforcement will increase and random inspection of vessels under 15 tons will be carried out.

The Department is now inspecting over 7 percent of all foreign ships and intends to meet the goal of 25 percent in 1990. Adherence to the European Port State Control Agreement, compulsory reporting through the Vessel Traffic Management system and the conduct of port warden surveys will provide a practical level of foreign ship control.

Safe operation of ferries is an international concern and the Department and Canadian Industry have recently contributed to new international guidelines.

Marine Emergencies

Background

22.39 The stated objective of the Marine Emergencies Branch is to "mitigate the effects of ship-source pollution". In 1989-90, the Branch estimates it will use $4.7 million and 63 person-years. The Canada Shipping Act gives the Department of Transport the authority to remedy, minimize or prevent pollution damage originating from a ship. Although the Act states that a polluter is liable for the cost of a clean-up, in practice, in an emergency situation not all polluters are capable of cleaning up polluting substances or of paying for the costs of the clean-up. Under the Act, the Minister may authorize the Department to ensure that the clean-up takes place and to recover costs from the polluter. Annually the Coast Guard reports there are 20 to 50 prosecutions of marine pollution violators, on the basis of information from Ship Safety Branch Inspectors. Levels of fines are determined by the courts. Recently, the Coast Guard reports maximum penalty provisions of the Canada Shipping Act have been increased from $100,000 to $250,000 per pollution incident.

22.40 Dangerous goods include explosives, compressed gases, flammable liquids or solids, poisonous substances, radioactive materials, and corrosives. Quantities of dangerous goods shipped through Canadian waters increase from year to year. There has been a growing public awareness and concern about the likelihood of accidents, potential damage from hazardous substances and the limitations of clean-up efforts. Exhibit 22.2, Transport of Hazardous Materials in Canadian Waters, illustrates estimated annual shipments by region. The source of these data, a recent study undertaken by the Coast Guard, also estimated that 40 percent of these reported shipments were oil based products and 60 percent were other types of hazardous materials.

22.41 Many regulations and Acts of Parliament exist to control the handling and shipment of dangerous goods. Domestic shipment of dangerous goods is regulated by the Transportation of Dangerous Goods Act, which seeks voluntary compliance on the part of shippers of dangerous goods. The transportation of dangerous goods involves various modes of transportation and is subject to federal and provincial jurisdictions. The Coast Guard states that, for the most part, Canada's regulations conform to international standards and regulations for transporting dangerous goods to or from other countries. Although legislation does not require that the safe packaging, labelling and transportation of all dangerous goods be verified through inspections, the Coast Guard has the authority to do so at its discretion.

22.42 The essence of a good prevention and response capability is extensive front-end analysis, identifying the risks and the knowledge, co-ordination, skills, materials and equipment that would be needed to respond. This analysis should form the basis of proper response plans which clearly set out the roles, responsibilities and jurisdictions of all parties as well as the procedures to be followed in the event of a marine emergency.

Audit Scope

22.43 As illustrated in Exhibit 22.3, "Marine Emergency Planning Systems Model", our examination focussed on the Coast Guard's contingency planning and its capability to deal with marine emergencies arising from the transportation of dangerous goods through Canadian waters. We did not examine the roles and capabilities of other participants in the joint response network.

Observations and Recommendations

22.44 We looked at two aspects of marine emergencies -- pollution prevention and containment and clean-up.

22.45 **Prevention procedures incomplete.** Given current limitations of the technology for containment and clean-up, prevention of pollution is of paramount importance. This can be achieved through education, and by ensuring that petroleum and chemical products including dangerous goods are packed (in the case of packaged goods), handled, stored

TRANSPORT OF HAZARDOUS MATERIALS IN CANADIAN WATERS
ESTIMATED ANNUAL SHIPMENTS

Geographic Regions	Total Number of Vessels with Hazardous Materials	Total Tons of Hazardous Materials Shipped
East Coast, North Atlantic and St. Lawrence River Region	6,150 - 8,180	38,600 - 53,830
Great Lakes Region	4,902 - 5,491	21,700 - 28,655
West Coast Region	2,405 - 3,130	22,785 - 30,435
Arctic Waters Region	290 - 445	1,040 - 1,260

SOURCE Canadian Coast Guard Marine Emergencies Branch, "Counter Measures for Marine Spills of Hazardous Materials: Phase I - Risk Analysis" March 1988

Exhibit 22.2

and transported safely. The Coast Guard has issued a large number of regulations to this effect but, except for the inspection of tankers, there is very limited enforcement activity to ensure compliance with the regulations. As in other situations, the Coast Guard relies on voluntary compliance with regulations but has done limited verification to demonstrate that this reliance is justified.

22.46 The Coast Guard states that the Ship Safety Branch places a high priority on the inspection of foreign tankers on their first visit to Canada each year. We noted that the Coast Guard has few other clearly articulated plans that determine the resources required for various discretionary ship safety activities in this area. Other inspection activity is limited to mandatory requirements.

22.47 In the Maritimes Region, the Ship Safety Branch reports that it inspects approximately 2 percent of the containers used in the transportation of dangerous goods. The Region monitors the movement of dangerous goods in its area and uses the information to determine which containers to inspect. The Region was not aware of any random inspections carried out on regular ferry runs to detect unlawful transportation of dangerous goods.

22.48 Although the Western Region each year does approximately 100 inspections of shipments of dangerous goods, it has no procedure for selecting a certain proportion of such shipments for random inspection, and it does no random inspection of ferries in the Region.

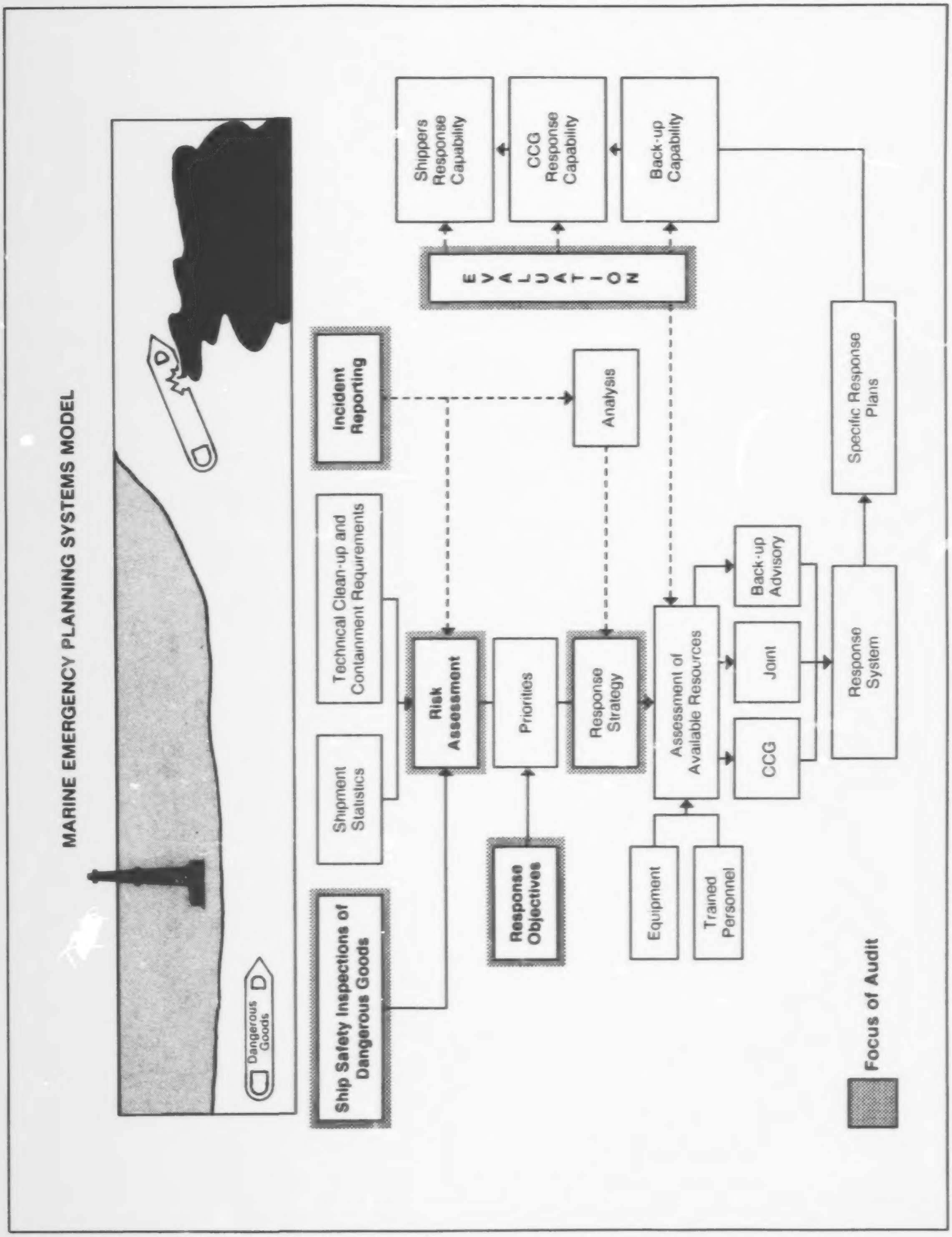

MARINE EMERGENCY PLANNING SYSTEMS MODEL
Dangerous Goods
Ship Safety Inspections of Dangerous Goods
Shipment Statistics
Technical Clean-up and Containment Requirements
Incident Reporting
Risk Assessment
Priorities
Response Objectives
Response Strategy
Analysis
EVALUATION
Assessment of Available Resources
Equipment
Trained Personnel
CCG
Joint
Back-up Advisory
Shippers Response Capability
CCG Response Capability
Back-up Capability
Response System
Specific Response Plans
Focus of Audit

Exhibit 22.3

22.49 In the Laurentian and Central Regions, the Branch reports it does virtually no inspection of dangerous goods shipments other than those on tankers.

22.50 We concluded that the senior management of the Coast Guard does not have reasonable assurance that its prevention activities are succeeding or that the risks to marine environment are being minimized.

22.51 The Coast Guard should clearly set out its objectives, roles and plans for preventing marine pollution and should allocate its resources accordingly.

At present, the Coast Guard has not developed the capability to deal with spills or accidents involving hazardous materials other than petroleum products, and there is no reasonable assurance that it would succeed in doing so.

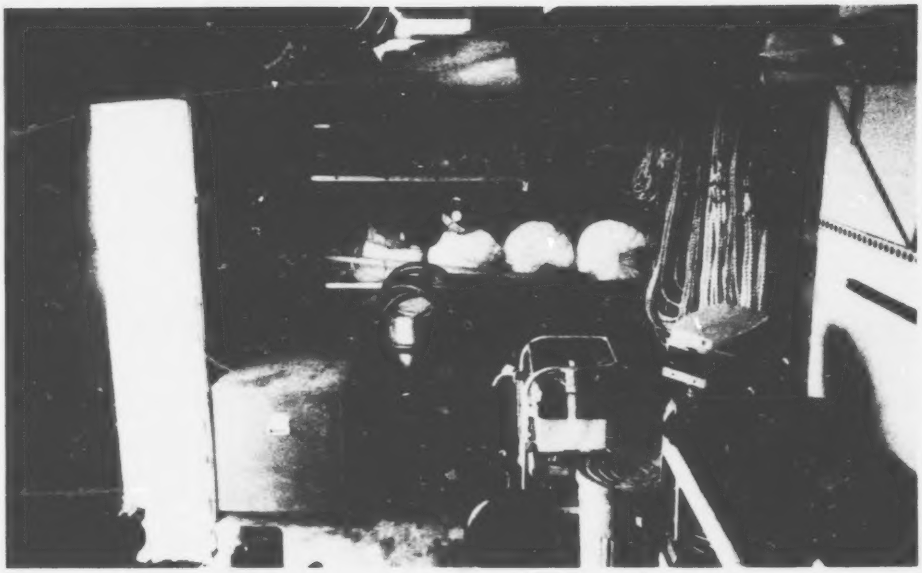
22.52 Gaps in containment, control and clean-up capability. The Coast Guard has stored oil pollution response equipment at 51 locations throughout the country, much of which is mobile and can be readily transported to the site of an oil spill. Contingency plans are in place for dealing with major oil spills and, in the case of waters contiguous to the United States, joint contingency plans exist. The Coast Guard states that these plans are regularly exercised to ensure that key personnel are effectively trained and that the necessary equipment and communications are readily available at the scene. The Coast Guard has gained some experience in containing and cleaning up oil spills. There is a network of agencies that provide mutual support and share facilities, which could be activated in the event of a major incident of oil pollution from a ship. However, neither the individual capabilities of participants in this network to field a response team, nor the full capability of the network, have been put to the test by a major oil spill.

22.53 In 1988 the Coast Guard carried out a preliminary risk assessment, which analyzed major categories of hazardous chemical shipments and identified technical requirements for responding. However, it has not articulated its objectives for clean-up and containment nor defined the areas of its jurisdiction.

22.54 At present, the Coast Guard has not developed the capability to deal with spills or accidents involving hazardous materials other than petroleum products, and there is no reasonable assurance that it would succeed in doing so, for the following reasons:

- There are dangerous products such as toxic chemicals which may dissolve if spilled in water. We were informed by the Coast Guard that there is little, if anything, that could be done to clean these up with existing technology.
- Current procedures and criteria for calling upon outside resources to deal with these spills are not clearly set out in the Coast Guard's contingency plans.
- Backup capabilities of other government departments and resources of commercial contractors are not clearly identified or described. For example, contingency plans contain lists of contractors, but their capabilities are not clearly articulated.
- The Coast Guard states it is not within its mandate to pre-inspect the capabilities of other organizations in the cooperative network. Consequently, contractors and other organizations have not been evaluated or inspected to establish the range of their backup capabilities to deal with dangerous materials spilled into a marine environment.

Oil pollution response equipment is stored throughout the country (see paragraph 22.52).



- Few of the mutual assistance arrangements and joint-response plans address hazardous materials other than oil products.

- The Coast Guard does not have a data base on the capability of shippers to deal with spills of hazardous materials.

22.55 The Coast Guard should establish the information base required, ensure that its contingency plans would meet the hazards identified and monitor the ability of shippers and the co-operative network to ensure that they can carry out their assigned roles.

***Departmental response**: The Department agrees with the recommendations in paragraphs 22.51 and 22.55 and will assess how to best increase inspections under the International Maritime Dangerous Goods Code, noting that shipping is only one link in a multi-modal transportation chain, and that implementation is rendered difficult by a wide variety of packaging, labelling and containment systems. A very sophisticated inter-agency and international effort is required to protect against dangerous commodities from the point of origin to the point of final disposal.*

On a global basis, there is at present no available technology that can fully mitigate the adverse effects of oil spills, particularly in the open ocean environment. A state-of-the-art readiness continues, however, to be actively pursued by the Department. Currently, the most effective defense against oil spills and the more complex spills of hazardous materials is to prevent their occurrence, by ensuring that ships carrying these substances are designed, manned and equipped and operated in accordance with accepted standards. These objectives are being addressed through the Department's work in support of the International Maritime Organization, as most vessels operating in Canadian waters are of foreign flag.

23

DEPARTMENT OF TRANSPORT - CANADIAN COAST GUARD

Fleet Management, Aids to Navigation and Icebreaking

23

DEPARTMENT OF TRANSPORT - CANADIAN COAST GUARD

Fleet Management, Aids to Navigation and Icebreaking

Main Points

23.1 **Fleet Management.** In our opinion the use of more efficient manning, maintenance and deployment practices could have a positive impact on the $183 million projected operating costs, and the $2.5 billion replacement costs, of the 46-vessel fleet. For most of its vessels used year-round to tend navigational aids and break ice, the Coast Guard uses an office-type work week rather than a system which would facilitate making the most efficient use of its ships. In our opinion overtime costs of $13.8 million could be reduced if compensation practices better matched the seasonal work patterns of its heavy icebreakers. Our analysis of fleet deployment indicated that the aids to navigation workload for 1987-88, a typical year, could have been done with at least five fewer ships, with no discernable reduction in present service. These ships have a replacement value of $169.1 million and annual operating costs of over $10 million (paragraphs 23.12 to 23.36).

23.2 **Aids to Navigation.** We found wide variations in the contracting out practices among regions for placing and maintaining buoys and other aids to navigation. We found examples of new technologies that had been developed in individual regions, but there was little cross-fertilization of these ideas among regions (23.47 to 23.54 and 23.65).

23.3 The Coast Guard has standardized the equipment used across the country, but we noted that few maintenance practices had been standardized. Consequently, one of the main benefits of standardization, improved efficiency, was not being achieved (23.55 to 23.58 and 23.65).

23.4 **Icebreaking.** The Coast Guard does not know the extent to which its existing fleet meets or exceeds program requirements. In spite of this lack of information and analysis on requirements, the Coast Guard has spent approximately $686 million in acquiring or modernizing vessels capable of undertaking icebreaking missions since our last audit in 1983 (23.72 and 23.83).

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Icebreaking

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DEPARTMENT OF TRANSPORT - CANADIAN COAST GUARD

Fleet Management, Aids to Navigation and Icebreaking

Introduction

23.5 To understand the Coast Guard, it is important to dispel some commonly held myths. The first myth is that the Coast Guard is a paramilitary body that polices the coast. In fact, Coast Guard ships are not armed and their crews are not trained in the use of firearms. The second myth is that the Coast Guard is a service much like the army or navy. In fact, the Coast Guard is a branch of the Department of Transport. The third myth about the Coast Guard is that it is heavily involved in the interdiction of illegal drugs, smugglers, illegal immigrants and other such activities. In fact, the Coast Guard has no legal mandate for such activities. The last myth about the Coast Guard is that there is one national fleet. In fact, fleet operations are highly decentralized and there are five regional fleets, each deployed, maintained and operated on a regional basis.

23.6 Two of the Coast Guard's primary functions are the aids to navigation and icebreaking programs. These programs directly and indirectly affect the lives of millions of Canadians, including remote communities in the North that rely on the annual Arctic Sealift for supplies and fuel. They also include commercial shipping companies which require assistance to navigate ice-filled waters and depend on aids to navigation to prevent marine casualties, commercial fishermen and pleasure boaters dependent on fixed and floating aids to marine navigation. A fleet of 46 ships, ranging from small buoy tenders to large Arctic class icebreakers, is used to support the aids to navigation and icebreaking programs.

23.7 The annual operating costs of the Coast Guard fleet for 1989-90 are estimated to be in excess of $183 million. At present there is no regime in place to recover these costs from users. The Department of Transport is in the midst of a major expenditure reduction exercise which has led to increased competition among the branches of the Department for capital and operating funds; every dollar allocated by the Department of Transport to the Coast Guard is a dollar that is not available for the air or surface transportation programs. We examined how the Coast Guard responds to user needs and the challenge of making the most efficient use of its resources.

Audit Scope

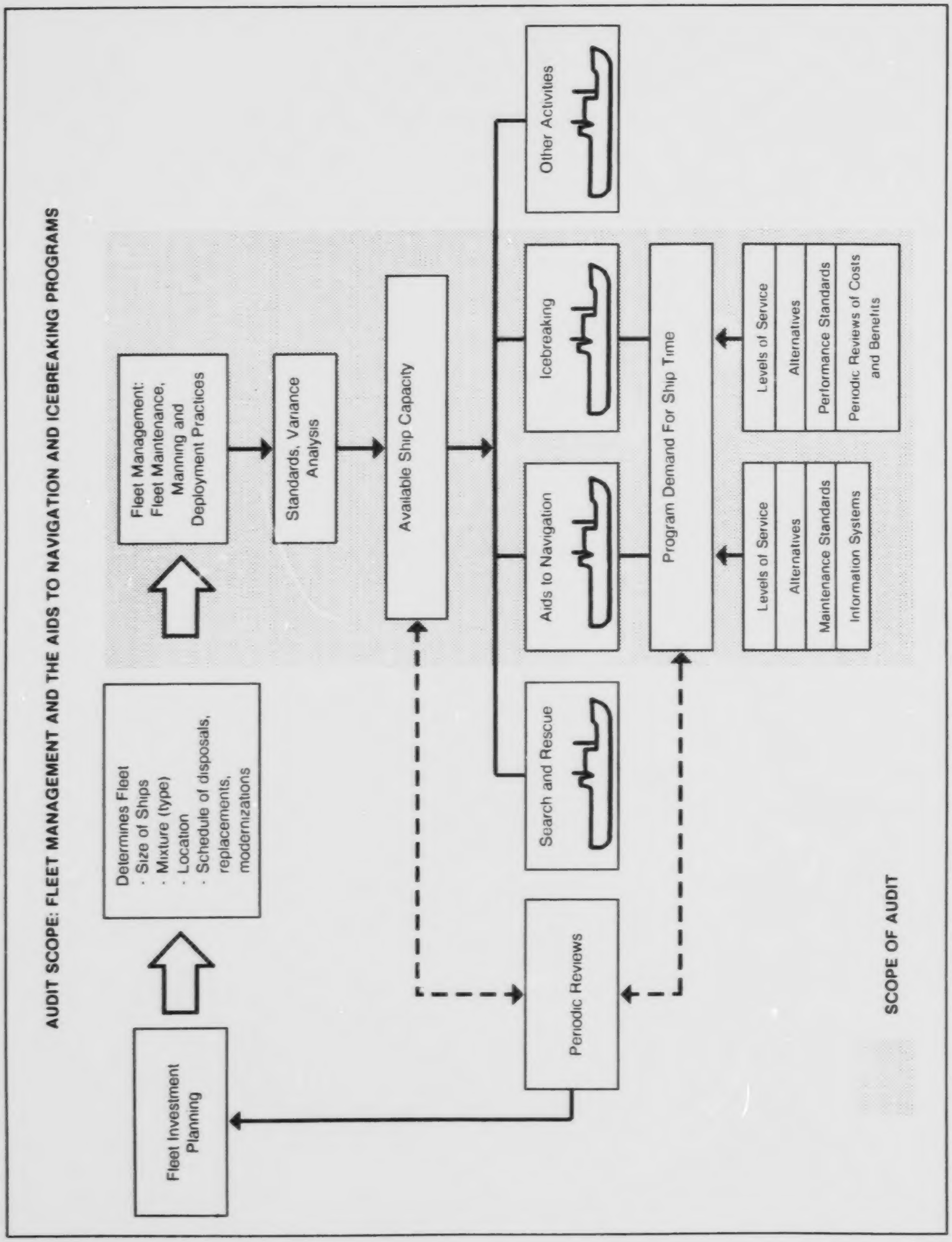
23.8 Exhibit 23.1 shows the scope of our examination of fleet management, as well as of the audit as a whole. The current audit excluded search and rescue, the management of harbours and ports, fleet acquisition and an examination of such major capital projects as the Polar 8 Icebreaker or the modernization of the Louis S. St. Laurent. These will be audited and reported later. The current status of the Polar 8 project is that it is not to proceed to the construction stage without reconsideration by Cabinet.

Fleet Management

Background

23.9 Exhibit 23.2 shows the size, location and capital cost of the fleet. The smaller, shallower draft vessels in the 700 to 900 classes are primarily used to tend aids to

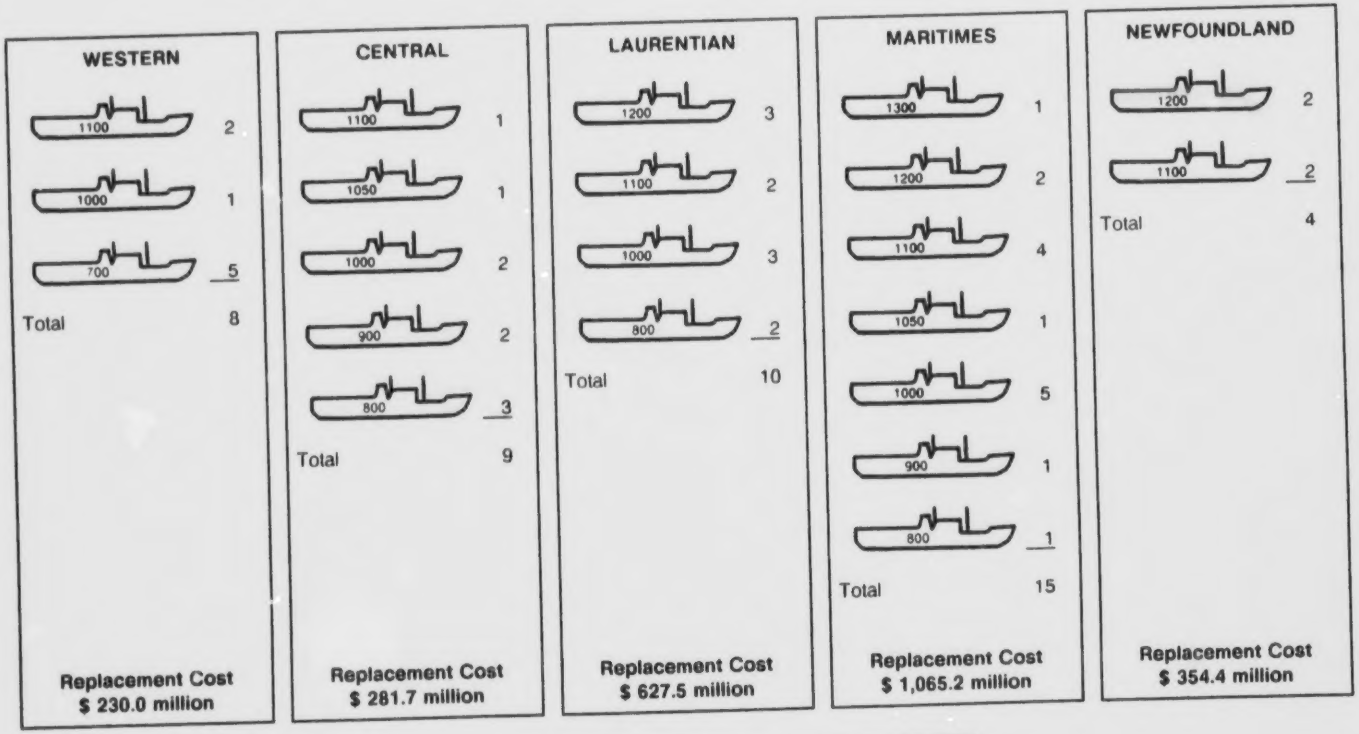
Exhibit 23.1



AUDIT SCOPE: FLEET MANAGEMENT AND THE AIDS TO NAVIGATION AND ICEBREAKING PROGRAMS

Fleet Investment Planning
Determines Fleet
· Size of Ships
· Mixture (type)
· Location
· Schedule of disposals, replacements, modernizations
Fleet Management: Fleet Maintenance, Manning and Deployment Practices
Standards, Variance Analysis
Available Ship Capacity
Periodic Reviews
Search and Rescue
Aids to Navigation
Icebreaking
Other Activities
Program Demand For Ship Time
Levels of Service
Alternatives
Maintenance Standards
Information Systems
Levels of Service
Alternatives
Performance Standards
Periodic Reviews of Costs and Benefits
SCOPE OF AUDIT

THE COAST GUARD'S AID TO NAVIGATION AND ICEBREAKING FLEET – BY CLASS AND REGION



WESTERN

1100	2
1000	1
700	5
Total	8

Replacement Cost
$ 230.0 million

CENTRAL

1100	1
1050	1
1000	2
900	2
800	3
Total	9

Replacement Cost
$ 281.7 million

LAURENTIAN

1200	3
1100	2
1000	3
800	2
Total	10

Replacement Cost
$ 627.5 million

MARITIMES

1300	1
1200	2
1100	4
1050	1
1000	5
900	1
800	1
Total	15

Replacement Cost
$ 1,065.2 million

NEWFOUNDLAND

1200	2
1100	2
Total	4

Replacement Cost
$ 354.4 million

TOTAL FLEET	**46**
REPLACEMENT COST	**$ 2,558.8 million**

Exhibit 23.2

navigation; in the 1000 to 1100 range, they are multi-tasked vessels capable of both tending aids and breaking ice. Vessels in the 1200 and above class are heavy icebreakers used in the St. Lawrence River, the Gulf of the St. Lawrence and Arctic operations.

23.10 The fleet is managed on a regional basis by the Fleet Systems organization, which is the largest component of the Coast Guard. At Headquarters, the Fleet Systems organization is responsible for setting national standards and providing functional direction on manning, deployment, maintenance and other logistics. The regional and district Fleet Systems organizations make the day-to-day deployment decisions.

23.11 Coast Guard vessels undertake a number of different types of missions: servicing, maintaining and constructing floating and fixed radio aids; sounding; icebreaking and escorting; ice management and flood control; Arctic resupply; Search and Rescue; pollution control and marine emergencies. The Coast Guard also supports departments and agencies such as the Canadian Hydrographic Service, the Department of the Environment, the Department of Fisheries and Oceans, Teleglobe Canada, the St. Lawrence Seaway Authority and law enforcement agencies.

Opportunities exist to improve the efficiency of fleet manning practices

23.12 Our examination focussed on whether the Coast Guard was using the most cost effective manning systems and on how overtime was managed. Given the standardization of the fleet and the increased use of multi-tasked vessels, we expected to find crewing systems that matched work requirements.

We examined how the Coast Guard responds to user needs and the challenge of making the most efficient use of its resources.

23.13 The Coast Guard uses two different systems in operating its icebreaking and navaids fleet: the conventional manning system and the lay day system. The conventional system follows normal office hours -- eight hours a day, five days a week, Monday to Friday. Time worked in excess of standard time is compensated at a higher rate of pay. Normally, Coast Guard ships return to their home ports for weekends and public holidays.

23.14 The lay day system is based on a continuous work period of 28 days followed by a leave period of 28 days. During the 28-day work period, each crew member works 12 hours each day, seven days a week. Under the lay day system, more person-years are required to operate the vessel, but the ship is available for use 24 hours a day, seven days a week. This optimizes the availability of the vessel and in the long run will reduce the number of vessels required. In normal operating conditions, overtime is not incurred. Under a conventional system, however, once a crew member works beyond his or her 40-hour work week, overtime is incurred. The Coast Guard states that a constraint it faces in implementing the lay day system is that it must obtain the agreement of the unions and that, in one region, the unions have not agreed to its implementation. To date it has converted 5 of the 36 multi-tasked ships in its aids to navigation and icebreaking fleet for which the lay day system would be appropriate.

23.15 We compared the manning systems for three navaids vessels in the Maritimes Region for 1987-88. As shown in Exhibit 23.3, the Earl Grey, operating on the lay day system, not only costs less but was used more than two conventionally crewed ships.

23.16 In the Newfoundland Region, use of the lay day system on the Sir Humphrey Gilbert and the Ann Harvey contributed to reducing the regional fleet by one vessel. While there are two ships on the lay day system in this region, there is only one in the Maritimes Region and none in either the Laurentian or Western regions.

THE ADVANTAGES OF THE LAY DAY MANNING SYSTEM

Vessel	Age	Actual Crew Size	Salary and Overtime	Utilization
EARL GREY (Lay Day)	2	24	$ 863,000 (1)	4,301 Hours
TUPPER (Conventional)	29	36	$ 1,165,000 (2)	2,987 Hours
A. MACKENZIE (Conventional)	38	29	$ 992,000 (3)	1,216 Hours

(1) Includes overtime of $62,900
(2) Includes overtime of $434,200
(3) Includes overtime of $356,000

Exhibit 23.3

23.17 We concluded that greater use of the lay day manning system would increase the availability of existing vessels, decrease the salary costs and potentially reduce the number of vessels required by a region.

23.18 Overtime makes up a large percentage of the ships' crewing costs. In 1987-88, overtime costs for the fleet totalled $13.8 million. We noted that crews receive full pay by remaining on board while a ship is not operational. They do so even though they have accumulated and retained enough compensatory leave to cover periods during which the vessel is non-operational. The Coast Guard states that cashing in of compensatory time off represents adherence to the contract negotiated for the employees. However, we note that a letter of understanding with the union recognizes that "failure to accumulate sufficient compensatory leave credits to cover the anticipated (non-operational) periods could lead to employees being placed on off-duty status, resulting in a loss of pay for all or a portion of the non-operational period". By paying cash in lieu of compensatory leave and keeping the crews on board at full pay, rather than adhering to the terms of the letter of understanding, the Coast Guard is not managing its overtime in a way that is consistent with the seasonal work patterns of its heavy icebreakers.

23.19 For example, in 1987-88 the Des Groseilliers, crewed on the conventional manning system, incurred overtime costs of $758,700. We noted that the ship was not required for any operations for the 20 weeks when it was berthed at Quebec City (13 weeks) and in the Vickers Shipyard in Montreal (7 weeks). During this period, according to the Ship Activity Report, the vessel remained fully crewed and employees received their regular pay. In addition, most of the crew chose to receive cash for overtime accumulated, rather than

Opportunities exist to improve the efficiency of the manning practices on heavy icebreakers (see paragraphs 23.19 to 23.21).

compensatory time off when the ship was not required for operational purposes. This payment averaged $12,645 for each of the 60 crew members. The Coast Guard informs us that often the crew is involved in self maintenance during these periods.

23.20 We also noted that the Coast Guard had recently completed an internal study on manning levels on all Coast Guard vessels. This study observed that, especially for large icebreakers, current crewing levels were in excess of levels recommended in the study.

23.21 When icebreakers and other vessels are berthed for extended periods for maintenance, or are undergoing midlife modernizations, they continue to be fully crewed. For example, the Edward Cornwallis was in port mainly because of problems with its speedcrane for 20 weeks in 1987-88. In addition, it was unassigned for 17 weeks. We noted that during this 37-week period the ship remained fully crewed at an average weekly cost of $25,775.

23.22 We concluded that the Coast Guard is not managing its use of overtime and compensatory leave in a manner consistent with the seasonal work patterns of the fleet.

Coast Guard unable to monitor the efficiency of fleet maintenance

23.23 The Coast Guard has made substantial progress in standardizing the specifications for its fleet. For example, since 1983 it has replaced older ships with six modern class 1100s. We therefore expected to find that maintenance practices that are now routine would have been standardized. However, the Coast Guard has not issued maintenance standards, and as a result individual regions have developed their own practices. As shown in Exhibit 23.4, the percentage of time spent in maintenance status by regional fleets varies significantly.

23.24 Out-of-pocket maintenance costs for parts and work contracted out amounted to approximately $15.8 million. In addition, because vessels in maintenance status are usually fully crewed, there are substantial payroll costs. The Coast Guard does not separately track these payroll costs.

VESSEL MAINTENANCE TIME - BY REGION

1987-88

	No. of Ships	Average Age	% Utilization*	% Maintenance	Maintenance Costs**
Newfoundland	5	15.5	55.0	11.1	$ 3.2 million
Western	3	17.6	35.6	13.8	$ .9 million
Laurentian	10	10.5	34.5	21.1	$ 4.4 million
Maritimes	13	20.9	29.5	28.6	$ 5.5 million

* As a percentage of gross hours available (366 x 24 hours).

** Out-of-pocket costs only.

Exhibit 23.4

23.25 According to the Coast Guard's records, maintenance time is lowest in the Newfoundland Region where utilization is highest, and highest in the Maritimes Region where utilization is lowest. The Coast Guard has not developed a variance reporting system which analyzes these differences, for similar ships, on a national and a regional basis. Consequently it is unable to monitor the efficiency of its maintenance practices.

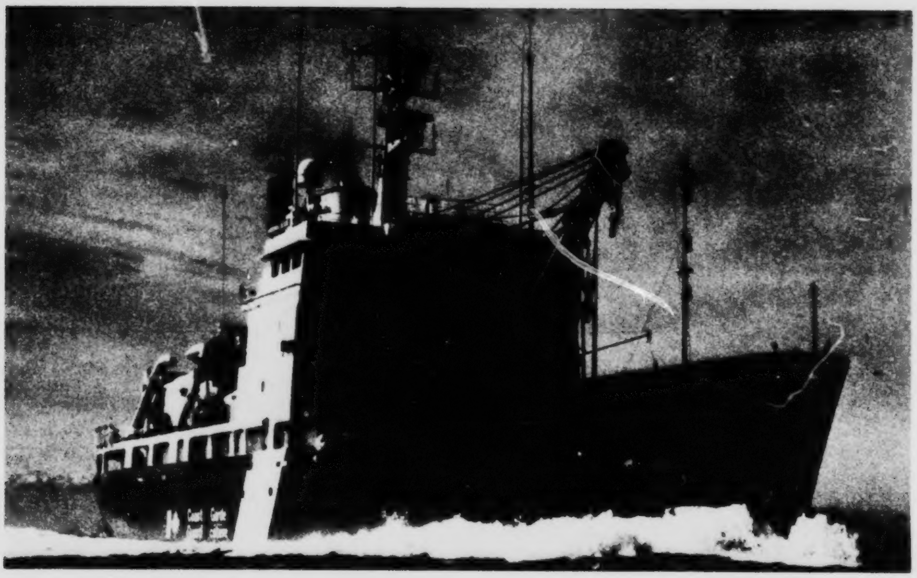
23.26 We concluded that, because of the lack of standards and reporting systems, senior management of the Coast Guard does not have assurance that maintenance is being carried out with due regard to economy and efficiency.

Evidence of excess capacity in the aids to navigation fleet

23.27 In the spring and fall each year, navaid vessels place and remove floating buoys. In the summer months they do construction work on aids in more remote areas. Fleet deployment is based on annual operational plans prepared by individual regions. These plans attempt to allocate the available tasks among the ships in the regional fleet for "blocked" periods of time.

23.28 The Coast Guard has developed a Ship Activity Reporting System to capture weekly information on the hours spent by a ship on program activities such as tending aids to navigation, icebreaking, or undergoing maintenance. The input for this system is a weekly report certified by the ship's Commanding Officer. From this data the system produces

Evidence of excess capacity in the aids to navigation fleet (paragraphs 23.27 to 23.35).



monthly reports which show utilization and maintenance, by ship. The data provide a profile of the ship's activities for each week.

23.29 However, we found that the Coast Guard was putting these data to limited use. For example, there was no comparison of total hours worked with total actual capacity in a region, which would provide the Coast Guard with the information it needs to improve efficiency and plan for vessel replacements. In addition, this would identify non-essential ships or shortages in the fleet and would be an improvement over the current practice of simply comparing forecasts.

23.30 We performed a basic analysis of actual regional capability for 1986-87 and 1987-88. We analyzed the availability of vessels against the actual hours worked for navigational aid tenders on a regional basis. For example, for the Maritimes Region, Exhibit 23.5 illustrates that for 1987-88 the fleet was underutilized every month in the year for a total of 13,373 hours. We then simulated the effect of removing one ship, the William, and distributing its workload among the remaining ships in the fleet. Our simulation suggested that the region would still have had excess capacity in every month of the year for a total of 10,499 hours for the year. We made the same kind of simulations using the Alexander Mackenzie and the Thomas Carleton, withdrawing them and distributing their workload among the other ships. Except for three months of the year which showed a combined shortfall of 242 hours, the regional fleet still had significant excess capacity.

23.31 This analysis is based on the assumption that, because of the high investment in the fleet and the seasonal nature of the navaids business, the navaid fleet would be available seven days a week during daylight hours.

23.32 Our analysis suggested that the 1987-88 peak period workload could be done with at least five fewer ships with no discernable reduction in the present service of the navaids program. The operating and replacement costs are illustrated in Exhibit 23.6.

23.33 We also considered what effect the removal of these ships would have on the icebreaking program in the region. Although 1987 was a particularly bad year for ice on the

MARITIMES REGION
1987-88
NAVAIDS FLEET - EXCESS CAPACITY

		HOURS REGIONAL VESSELS MINUS				
Month	**All Regional Vessels Excess (Shortfall)**	**William Excess (Shortfall)**	**Plus**	**Alexander Mackenzie Excess (Shortfall)**	**Plus**	**Thomas Carleton Excess (Shortfall)**
APR	874.10	552.50		290.48		25.50
MAY	982.05	648.95		336.85		(25.15)
JUNE	1,380.20	1,026.80		1,003.69		839.80
JULY	1,683.75	1,335.75		1,335.75		1,079.95
AUG	938.40	722.40		722.40		481.60
SEPT	934.25	574.25		357.85		11.55
OCT	1,451.85	1,231.85		859.85		521.85
NOV	1,377.80	1,377.80		1,139.69		1,139.80
DEC	1,503.60	1,377.45		1,095.55		1,006.15
JAN	568.90	320.50		158.47		(144.40)
FEB	880.10	689.40		403.40		71.70
MAR	798.05	641.80		287.77		(72.20)
1987-88	**13,373.05**	**10,499.45**		**7,991.75**		**4,936.15**

Exhibit 23.5

east coast, the ships we identified as non-essential contributed very little to the icebreaking programs of those regions during the year.

23.34 The purpose of our analysis, which was fairly basic, was to demonstrate the kind of reports senior managers and planners could be provided with, using the Coast Guard's current systems and data base. Based on the needs of management, a number of additional variables and further sophistications could be introduced. The essential point, however, is that analyses of this type would improve the information available to senior decision makers in the Coast Guard. We concluded that there is an urgent and ongoing need for the Coast Guard to strengthen its analytical capability so that it can properly analyze its regional program requirements and capacity and provide complete information to senior management for making decisions on deployment, replacement or modernization.

23.35 The Department has prepared a draft plan for fleet capital investment which states that four ships will be decommissioned without replacement by 1992.

23.36 The Coast Guard should:

- **explore opportunities to increase vessel availability through implementation of the lay day manning system on appropriate vessels, as well as implementing a compensation system appropriate to both the seasonal nature of the Coast Guard's work and its demanding operational requirements;**

COST OF NON-ESSENTIAL SHIPS

Region	Non-Essential Ship (Type)	Age (Years)	Annual Operating Cost	Replacement Cost	
Laurentian Region					
	J.E. Bernier (1100)	21	$ 3.44 million	$ 66.3 million	(1)
	Montmagny (1000)	25	1.35 million	51.4 million	(2)
Maritimes Region					
	William (1100)	29	2.33 million		(3)
	Alexander Mackenzie (1000)	38	1.47 million		(4)
	Thomas Carleton (1000)	28	2.34 million	51.4 million	
			$10.93 million	$169.1 million	

(1) Scheduled for midlife modernization in 1989 at an estimated cost of $10.1 million.
(2) Scheduled for replacement in 1991.
(3) Scheduled for decommissioning in 1989.
(4) To be decommissioned without replacement.

Exhibit 23.6

- **develop maintenance standards and monitor variances for better control over maintenance costs; and**
- **strengthen its ability to analyze regional program needs for the icebreaking and aids to navigation fleet and provide complete information to senior management for decisions on planned ship modernizations or replacements.**

Department's response: *The Department has significantly reduced the number of vessels in the Icebreaking and Navaids fleet from 52 vessels in 1983-84 to 46, and will further reduce to 42 vessels by 1993, a decrease in numbers of vessels by 18 percent in a decade. Fleet capacity is analyzed by the Department to meet regional and national transportation and safety objectives, and opportunities to utilize any excess operational capacity are explored with other government departments requiring fleet support.*

The Department will further explore lay day (24 hours) manning and will examine options for compensation, noting that further implementation of the lay day system is subject to union agreement and operational considerations.

Aids to Navigation

Background

23.37 The objective of the aids to navigation program is to ensure that a national marine navigation system is provided, operated and maintained to contribute to the safe, efficient and economical movement of vessels in Canadian and designated international waters. The aids to navigation program is an essential service that the Coast Guard has provided to Canadian mariners and the international marine community for decades.

23.38 At 31 March 1988, the Coast Guard was responsible for placing and maintaining 12,649 floating aids, 2,899 of which were lighted. Floating aids are used to warn vessels of hazards such as rocks or shoals, to mark navigable channels, to indicate harbour entrances, and to mark anchorage areas. The Coast Guard was also responsible for 9,629 fixed aids situated along the mainland and island shorelines. Since our last audit there has been a five percent overall reduction in the number of aids to navigation.

23.39 The cost of acquiring these short-range aids to navigation is very small compared with their maintenance costs. The replacement value of a small steel buoy is approximately $200 and of the largest steel buoy about $13,000. The small buoy will last between 3 to 5 years, while the life expectancy of a large buoy is 30 years or more.

23.40 In 1988-89 provision of short-range aids to navigation will account for $141.4 million. Over 50 percent of that amount, or $83.1 million, relates to the operating costs of the vessels used to place the buoys and verify their position and operating condition. Each buoy is checked at least twice a year, and the operating costs of a navaids tender range from $220 an hour worked to $2,100 an hour worked.

23.41 The delivery of the Coast Guard's operational programs such as Aids to Navigation is accomplished through a decentralized framework of regional and district offices. The Department states that this decentralized approach is necessitated by Canada's vast diversity in geographic and climatic conditions. While we anticipated that this diversity would be reflected in Coast Guard operations, we also expected that Coast Guard practices would maintain a reasonable balance between regional differences and the need to standardize practices for similar activities, in similar types of environments, using similar types of equipment.

No national levels of service

23.42 In 1974, the Treasury Board identified the need for the Coast Guard to define levels of service and in 1983, we observed that little had been achieved in this area. While we recognize this is a very complex task, and the Coast Guard appears to have intensified its efforts in recent years, it still does not have defined levels of service, or a standard approach to defining the need for these short-range aids. In the absence of defined levels of service, it has implemented cyclical reviews, developed a needs determination manual and conducted pilot tests.

23.43 Cyclical reviews according to existing policy consist of desk top analysis based on professional knowledge and expertise of Marine Aids managers followed by meetings with the users to determine whether a particular aid is required. What is missing from this process is a set of criteria for retaining, deleting or enhancing aids. Criteria such as the minimum number of users, risk and danger factors, and life-cycle costs to position an aid would ensure that these reviews were consistent. This would contribute to an equitable and cost-effective service.

23.44 The Coast Guard is presently proceeding with the revision of its policy on cyclical review to include criteria such as: type, size, number of vessels, weather and sun conditions, aids characteristics, previous incidents, reviews and users' requests as well as cost comparisons. This will contribute to an equitable and cost effective level of service.

23.45 In its current expense reduction exercise, the Department of Transport has to make resource allocation decisions among competing demands. Clearly defined levels of service and consistent application of cyclical reviews will make such decisions easier.

23.46 We also looked at current maintenance practices, focussing on how well cost-effective alternatives are considered for delivering the existing program.

Alternative methods of program delivery not fully exploited

23.47 In a time of restraint and cost reductions, we expected to find an emphasis on exploring economic and efficient methods of program delivery. The Coast Guard has made some efforts and achieved some success in a few areas, but it does not have either a formal process or criteria for assessing alternatives.

23.48 For example, there is no overall Coast Guard policy on when and how contractors should be used for placing and maintaining aids to navigation and no formal guidelines on contracting out. There is a wide variation in the use of contractors.

23.49 In the six districts we reviewed, of the 5,590 small and medium sized buoys, 2,873 are serviced by contractors and 2,717 are serviced by the Coast Guard. (Exhibit 23.7) A change in these contracting arrangements would have a significant impact on future regional ship requirements. No cost-benefit analysis has been done to determine the best mix between the Coast Guard and the private sector. The Coast Guard has not analyzed the wide variations in the contracting-out practices among the regions.

23.50 For the 1,260 large buoys in the six districts, no deployment and maintenance was contracted out. We were informed that limitations include the number of commercial fishermen interested in contracting and the lack of large ships in the private sector capable of handling the large buoys. However, we saw no evidence that the Coast Guard had attempted to formally solicit expressions of interest in this work from the private sector.

23.51 There is no reliable unit cost data on which to base a comparison of in-house and contract costs for similar activities. Our analysis shows that the average annual charge per buoy for maintenance by contractors is $200. While there are no precise cost figures available for in-house work, the average hourly cost for operating a Coast Guard vessel varies from $220 for a small vessel to $2,100 for a large vessel.

23.52 We found that the Coast Guard has conducted research on new technologies to reduce the cost of maintaining aids to navigation. There has been some implementation of these innovations, such as solar panels on fixed aids, low maintenance buildings, power generation, etc. However, although there are examples of innovations in individual regions, we found a number of situations where these innovations were not transferred to other regions.

23.53 An example of this is an innovative buoy mooring attachment that was designed and developed by the Laurentian Region in the early 1980s. At 31 March 1989, there were 1,234 electric buoys of the 6 and 9.5-foot size that could benefit from the new mooring attachment. An additional 708 electric buoys of the 4.5-foot size could be converted if trials prove successful. However, only 164 of all three sizes had been converted.

EXTENT OF CONTRACTING FOR
SERVICING OF BUOYS
1987-88

REGION/DISTRICT	Small	Medium	Total	Contract	Contract
Newfoundland	221	150	371	185	50%
Charlottetown	918	607	1,525	1,331	87%
Dartmouth	869	388	1,257	739	59%
Saint John, N.B.	531	343	874	47	5%
Laurentian	585	663	1,248	452	36%
Victoria	134	181	315	119	38%
Total	3,258	2,332	5,590	2,873	

Exhibit 23.7

23.54 The Coast Guard has been investigating using solar panels to recharge batteries since 1981. It reports that land-based solar conversion has progressed almost according to the original target dates. By 1990, the Coast Guard projects that 3,200 land-based minor aids will be on solar powered batteries. However, it has been slower to solarize floating buoys. The Coast Guard informs us that sealed batteries for floating aids have only been available for the past two years. Changing batteries can require the deployment of a vessel, so increasing their life from one year to as much as five to eight years could require fewer maintenance visits.

Lack of uniformity in maintenance standards

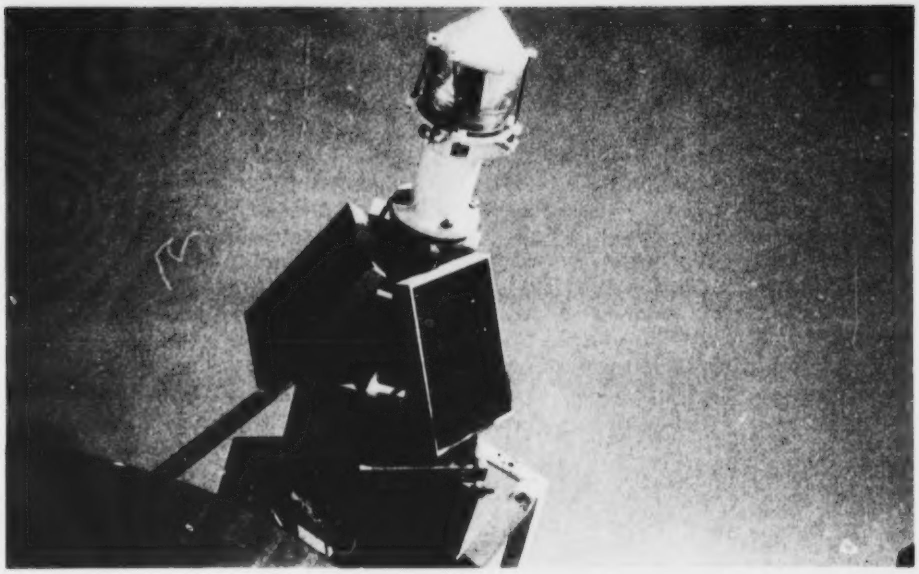
23.55 The Coast Guard has made an effort to standardize equipment across the country, using standard diesel engines, buoy designs and drycell batteries, for example.

23.56 However, few standard maintenance practices have been developed. For example, except for diesel engines, there is no uniform preventive maintenance system for standard equipment used under similar conditions. Guidelines for checking the operating conditions of fixed aids are general and incomplete As a result, maintenance practices in different districts varied quite significantly for the same type of equipment. For example, the Saint John District has developed and uses a detailed inspection checklist for lighthouses, while the Newfoundland Region follows no specific maintenance instructions. Generally, there was no consistency among regions about timing and procedures for inspecting equipment.

Limited transfer of innovations, like the Quebec mooring attachment, to other regions (see paragraph 23.53).

23.57 A good example of the lack of uniformity of maintenance practices is the painting of steel buoys. Although we understand that buoys in operation in an ice-infested environment will require different maintenance than buoys operating in milder climates, we expected that standard buoy painting practices could be developed for ice-infested, and non-ice environments. In the Newfoundland Region, steel buoys are painted with a high performance coating system which lasts at least three years. In Dartmouth and Charlottetown districts, they are sand blasted and painted annually. Buoys in the Charlottetown District, maintained by contractors, are scraped and hand painted yearly but not sandblasted. In Saint John District and the Laurentian Region, they are brought to shore yearly and also scraped and hand painted but not sandblasted. In Victoria District, they are cleaned, scraped and spot-painted yearly on board a vessel and put back into

The Coast Guard has made progress with land-based solar conversion but has been slower to solarize floating buoys (see paragraph 23.54).



service. The buoys are brought to the base on a five year rotational basis for a complete sandblasting and painting job.

23.58 The Coast Guard has developed national standards for frequency of buoy checking. However it does not have a quality control program to ensure that they are being properly applied. In the Laurentian and Newfoundland regions, for example, the frequency of inspections continues to be based on historical precedent, local practice and available resources rather than the national criteria, even though standards in their present form have been in place since 1985. We believe that the absence of strong quality control mechanisms leads to inconsistent application of the national standards. Managers in the regions need more information to ensure that maintenance operations are being carried out with due regard to economy and efficiency.

Need for information systems

23.59 The Coast Guard's objective is to contribute to a safe and efficient marine transportation system. On a day-to-day basis managers must make decisions on where and how to respond to equipment outages, position navigational aids, etc. To respond in the most effective and efficient manner, they not only need a response capability, but they also need a reliable information system to direct it. Such a system would provide an accurate and timely set of integrated financial and operating reports, so that management at each level would have the information to take corrective action if required.

23.60 The Coast Guard has been working on developing such a system since 1983. However, the system is still not fully operational. One region, on its own initiative, has developed a management information system that includes data on all fixed and floating aids to navigation and service records for the past three years. Using the data in this regional system we produced some basic analysis, for illustrative purposes only, to demonstrate the kind of information that could be made available to managers. It could be used to make decisions on frequency of maintenance, to highlight problem areas by showing where there are high outages or high out-of-position rates, etc.

23.61 For example, our analysis showed that

Little uniformity in painting practices for steel buoys (see paragraph 23.57).

- of the 220 outages reported, 33 percent were false alarms;
- 52 percent of the outages could be attributed to 7 percent of the buoys;
- one buoy received 17 service calls between September 1986 and September 1988.

23.62 Clearly this is the type of information a good manager would be interested in, and may be receiving by less formal means. Exhibit 23.8 provides another illustration of the type of report that could be made available. In this district all buoys are scheduled for at least two inspections a year, and every time there is a visit to a buoy, scheduled or unscheduled, a buoy service report has to be prepared.

SUMMARY OF SERVICE REPORTS FOR BUOYS
FROM 1 APRIL 1986 TO 31 MARCH 1988

No. of buoys with no reported visits (1)	119
No. of buoys with 1 reported visit	19
No. of buoys with 2 reported visits	22
No. of buoys with 3 reported visits	59
No. of buoys with 4 reported visits	59
No. of buoys with 5 reported visits	68
No. of buoys with 6 reported visits	36
No. of buoys with 7 reported visits	18
No. of buoys with 8 reported visits	13
No. of buoys with 9 reported visits	3
No. of buoys with 10 reported visits (2)	1
No. of buoys with 11 reported visits (2)	2
No. of buoys with 12 reported visits (2)	2
No. of buoys with 13 reported visits (2)	2
	423

(1) Was a service call actually made and a report not put in, or was there no service action?

(2) For those buoys with more than four service reports, why were there so many service calls? Are the frequency of maintenance standards unrealistic?

Exhibit 23.8

23.63 There may, or may not, be good reasons for the above occurrences. This is not the issue. The real issue is that, in the absence of such a report, managers' attention might not be drawn to these exceptions and, consequently, there might not be an investigation of their causes. A problem could thus fester for a long time and create a drain on resources.

23.64 Because managers in the regions we visited were not receiving exception reports highlighting the number and frequency of service visits, they may not have adequate information to investigate the causes of potential problems or to ensure that they were carrying out servicing operations in the most appropriate and efficient manner.

23.65 For the aids to navigation program, the Coast Guard should:

- **develop a formal process and criteria for assessing alternatives for delivery of the program such as contracting out for aids maintenance;**
- **provide a national focal point for dissemination and implementation of new technologies offering cost saving opportunities;**
- **standardize maintenance practices for fixed and floating aids for similar types of environments and ensure that national standards on the frequency of buoy maintenance are applied consistently in all regions; and**

- **complete the development of systems to provide line managers with the information required for day-to-day decisions on maintenance intervals.**

***Department's response**: The Department will further examine alternatives for program delivery through application of the Treasury Board's Guide on the approach to the most effective organization. Initiatives are under way to develop additional maintenance standards, and a more comprehensive information management system is under development.*

The Department has assigned the responsibility to Coast Guard headquarters to provide a national focal point for new technologies and to promulgate these technologies throughout the Coast Guard.

Icebreaking

Background

23.66 The mission of the icebreaking program is 1) to facilitate the safe and efficient movement of marine traffic through or around ice-infested waters; 2) to support marine related activities and other government objectives, including sovereignty in the Canadian Arctic; and 3) to minimize the effects of flooding caused by ice jams in the upper St. Lawrence River.

23.67 Icebreaking is a major activity of the Coast Guard that has evolved over the years. The biggest component of this program is route assistance for commercial shipping through ice-infested waters. The Coast Guard estimates that the program will consume $79.9 million and 866 person-years in 1989-90.

23.68 The Coast Guard's icebreaking activity takes place in three areas -- the Gulf of St. Lawrence, the Eastern Arctic and the Western Arctic. In the Gulf of St. Lawrence, it provides escorts and keeps major shipping lanes open for navigation from the Maritimes to Montreal during the winter months. It also opens harbours to expedite the movement of cargo and fishing vessels. Ice in the Gulf of St. Lawrence typically starts forming in early December and spreads eastward toward the Magdalen Islands. The peak of the icebreaking season in the Laurentian Region is in January and February, with demand typically diminishing in March. The peak in the Maritimes Region is normally in late February and March. These different peaks provide opportunities for staggered deployment.

23.69 Eastern Arctic operations involve co-ordination and icebreaker support for the sealift which provides food, materials, fuel and equipment to northern settlements and defence sites. Typically, the Eastern Arctic operations deploy six icebreakers. Unlike the Gulf, where it is difficult to anticipate vessel traffic in advance, much of the demand for Arctic escorts is identified by users each spring in an annual planning meeting. In the Western Arctic, one 1100 class vessel is deployed, principally to maintain aids to navigation and support shipment of supplies from Hay River to northern communities. The total cost of Eastern and Western Arctic operations for the 1987 season was approximately $30 million.

23.70 Icebreaking is an inherently expensive business. A heavy icebreaker has a crew of 60 or 70 -- its annual operating and maintenance costs generally average $5.5 million -- and its replacement cost is around $110 million.

23.71 It should be noted that there are various levels of icebreaking capability within the Coast Guard fleet. The following list gives the number of vessels in each type category, according to icebreaking capability:

(a) 8 ICEBREAKERS (Class 1200 and 1300) - large, powerful vessels with thick hulls which are designed and built solely for the purpose of icebreaking.

(b) 11 BUOY TENDERS/LIGHT ICEBREAKERS (Class 1100) - designed and built primarily to tend navigational aids, but have the capability to be multi-tasked and thereby perform light icebreaking duties, as a secondary function, in all areas including the sub-arctic.

(c) 13 BUOY TENDERS/LIGHT ICEBREAKERS (Class 1000 and 1050) - designed and built to tend buoys but are ice-capable or ice-strengthened; these vessels are lower powered, with shallow drafts and their capability in ice is severely limited.

32 Vessels capable of working in ice.

No national levels of service

23.72 In 1983 we noted that the need to provide icebreaker escort services had not been analyzed relative to either economic benefits or meeting other government objectives. While efforts are underway, levels of service have yet to be defined.

23.73 There are few natural limits to the icebreaking program. The Coast Guard states that all requests for service are considered valid. In theory, the Coast Guard could set a level of service objective of building a large enough fleet to escort every ship in Canadian waters during the ice season. Whether a ship does or does not need an escort largely depends on the judgment of the commanding officer or the ice officer. Also, there are large differences in ice conditions among regions and from year to year. There are no set workload factors as there are for the aids to navigation program. Icebreakers spend a high proportion of their time standing by, and the Coast Guard has not determined how much standby time is reasonable. Control is further complicated by the different icebreaking capabilities of the various ships and the year-to-year unpredictability of ice conditions.

23.74 The Coast Guard states that, in the absence of extensive planning systems, it depends heavily on the experienced professionalism and commitment to service of key managers. Considerable effort is expended to receive the views and criticisms of the marine industry.

23.75 Since there were no defined levels of service, we examined actual deployment practices to observe how deployment was controlled for the Gulf operations and the Eastern and Western Arctic.

Lack of cost-benefit analysis in Gulf operations

23.76 The Coast Guard has divided the area from Montreal to Newfoundland into three ice zones, each serviced by a separate region. The Laurentian, Maritimes and Newfoundland regions each have their own icebreaking fleets which they deploy according to the demands of vessels operating in regional waters. Typically, within a region, an icebreaker may be assigned to a specific geographic sector. However, the Coast Guard was unable to provide us with a national strategy for the three contiguous regions serving the Gulf, or a plan which treated the icebreaking fleet as one Eastern fleet whose deployment could take advantage of the differing regional peak periods.

23.77 In the Laurentian Region, for example, a 1200 class heavy icebreaker is stationed at Quebec from December to March primarily for flood control, a 1200 class vessel is deployed off Matane-Baie Comeau primarily to support a local ferry, and a new 1100 class vessel is deployed primarily in the Saguenay River area to support marine navigation in the winter. Deployment was largely based on ship availability. The Coast Guard was unable to provide us with an analysis which identified the minimum number of vessels necessary to provide the existing service, matched proposed deployment to anticipated ice conditions and vessel traffic patterns, analyzed alternatives to deploying Coast Guard vessels or compared the costs of providing the services with the benefits of year-round access to a given geographic area.

In summary, we concluded that the Coast Guard does not know precisely enough what its needs are for icebreakers. Given that each has a replacement value of up to $110 million and an annual operating cost of over $5 million, an overstatement of need by only one vessel would be costly.

23.78 We analyzed the use of the icebreaker provided to support the ferry in the Matane-Baie Comeau area from the beginning of January to the end of March 1988. Our analysis indicated that the deployment was continuous, but out of an ice season of 1,994 hours, the icebreaker spent 1,470 hours in standby status. In 1987-88 the cost of this level of service decision, using the daily rate for icebreakers deployed at Matane, was $2.7 million for the standby time alone. There was no formal process or rationale for selecting this, or any other site, over other sites in contiguous areas. The Coast Guard was unable to provide us with a front-end analysis of the costs and benefits of providing the service or an analysis of alternatives to the full-time deployment of an icebreaker.

23.79 The situation was similar in the Maritimes Region. There was no documented analysis which identified the minimum number of vessels necessary to provide the existing level of service. The Maritimes fleet contains 11 vessels capable of working in ice -- 3 icebreakers, 4 Navaid tenders with limited icebreaking capability, one ice strengthened vessel and 3 vessels restricted to open water unless absolutely necessary. Only 5 made a major contribution to the 1987-88 icebreaking season; yet, according to the Coast Guard's long term investment plan, all 11 are scheduled to be eventually modernized or replaced with vessels with enhanced icebreaking capability.

Alternative deployment strategies for the Arctic not explored

23.80 In the Eastern Arctic program in 1987, we found that seven ships were deployed for a total of 652 days. Exhibit 23.9 sets out the tasks the ships performed during the season.

23.81 We were informed that the Coast Guard's main objective is to maximize vessel availability in the Eastern Arctic. The Coast Guard continues to follow historic patterns of sending all available icebreakers to the Arctic every summer. As a result, they report that high standby time is an inherent cost of the program. However, without any obvious natural limits to possible service, a strong analytical capability is important if significant variable costs such as fuel and overtime are to be adequately controlled. The Coast Guard could not provide us with an analysis of whether its Arctic icebreakers on standby might be gainfully employed in such activities as Arctic hydrography or whether, through better scheduling, the number of vessels deployed could be reduced.

23.82 Each year, one of the Western Region's two 1100 class medium icebreakers is deployed in the Western Arctic, primarily to support the aids to navigation program, with incidental icebreaking assistance. The Coast Guard states that, with respect to Western Arctic tasking, the assigned ship's duties remain predominantly related to aids to navigation. The western ships are light icebreakers only and therefore are limited in the amount of ice escort duties they can perform in the severe conditions of the Arctic. Consequently, one 1100 is not available in the south for aids to navigation work during that

SUMMARY OF 1987 EASTERN ARCTIC ACTIVITY

Activity	No. of days	% of days
Days on standby	208	31.9
Days en route and returning	113	17.3
Days on escort duty	110	16.9
Other activities	104	15.9
Days on navaids work	63	9.7
Days on transit	54	8.3
Total	652	100.0
Total number of escorts		75
Total distance travelled		72,243 miles
Total fuel consumed		11,657 metric tons
Total cost of operations		$24.6 million

Exhibit 23.9

period. When we reviewed the utilization of the Western Region's Navaids and icebreaking fleet, we found evidence of significant excess capacity. The prospect of leasing icebreakers has been looked at a number of times by the Coast Guard, on both a short- and long-term basis, though not specifically for the western aids to navigation and icebreaking roles. The downturn in oil exploration in the early 1980s resulted in less activity for private icebreakers; they are available for tasks currently performed by the Coast Guard in the Western Arctic. We noted that the Coast Guard has not fully explored this possibility. Exploring this alternative could be timely, given the planned replacement by the Western Region in 1990 of the Class 1000 Douglas at a projected cost of at least $33.4 million.

Fleet replacement needs are not clearly defined

23.83 The Coast Guard has spent about $686 million on the acquisition and modernization of vessels in the 1000-1300 classes since 1983. Currently, it is projecting an expenditure of $95 million on modernizing the Class 1300 Louis S. St. Laurent and $10.1 million on the Class 1100 Bernier, neither of which have played a major role in the icebreaking programs of their regions in the past five years. In the absence of defined costs, benefits and levels of service, we concluded that it is impossible to determine the impact on the icebreaking program of including or excluding these vessels. At present the Coast Guard has 32 vessels capable of working in ice. Yet when we looked at regional utilization for 1987-88, which was a heavy ice season, we found that only 13 out of 28 vessels in the regions we examined made a substantial contribution to the icebreaking program. The Coast Guard

Icebreaking fleet's replacement needs are not clearly defined (see paragraph 23.83).

states that to provide icebreaking assistance, eight heavy icebreaking vessels are employed and complemented by those aids-to-navigation vessels that have icebreaking capability.

23.84 In summary, we concluded that the Coast Guard does not know precisely enough what its needs are for icebreakers. Given that each has a replacement value of up to $110 million and an annual operating cost of over $5 million, an overstatement of need by only one vessel would be costly.

23.85 The Coast Guard should develop criteria and procedures for analyzing competing demands for icebreaker deployment and setting priorities to ensure that its vessels are deployed where needed most.

Department's response: *The Levels of Service Framework, presently under development, will address the Auditor General's concerns. The Department notes that this has been a complex task due to variability of service demands, annual weather/ice conditions, and geographic diversity.*

24

CANADA EMPLOYMENT AND IMMIGRATION COMMISSION

Unemployment Insurance Account

24

CANADA EMPLOYMENT AND IMMIGRATION COMMISSION

Unemployment Insurance Account

Main Points

24.1 The Unemployment Insurance Program has evolved over the years into a compulsory and contributory socio-economic program as well as an insurance program. However the regular benefits paid relating to the insurance objectives and to the socio-economic aspects are not subject to separate disclosure to Parliament (paragraphs 24.12 to 24.17).

24.2 The Commission continues to detect a large number of overpayment cases each year These represent 12 percent of all claims for benefits. Until recently, few initiatives had been undertaken for purposes of deterrence or prevention (24.26 to 24.30).

24.3 Because detection of infractions is late, penalties are weak, and overpayments are not recovered from money owed to claimants by other federal programs, there are few effective deterrents (24.31 to 24.41).

24.4 A lack of indicators to assess the performance, speed, and quality of counselling services and their effectiveness makes them difficult to manage (24.66 to 24.80).

24.5 Potential cost savings could be achieved by further reducing general administration and support services costs chargeable to the UI Account (24.84 to 24.92).

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CANADA EMPLOYMENT AND IMMIGRATION COMMISSION

Unemployment Insurance Account

Introduction and Audit Scope

24.6 The Unemployment Insurance (UI) Program is a social insurance program intended to protect workers in Canada from loss of employment income. It provides temporary income support to unemployed workers while they seek employment or if they are unable to work because of sickness, disability, pregnancy or adoption of children.

24.7 In 1988, over 13 million workers and some 1.1 million employers contributed $11.8 billion to the Unemployment Insurance Account, in addition to the $2.7 billion contributed by the government. Approximately $10.8 billion in UI benefits were paid to nearly three million beneficiaries. Total administration costs charged to the UI Account amounted to $974 million (See Exhibit 24.4).

24.8 The Canada Employment and Immigration Commission administers the Unemployment Insurance Act, 1971. The Commission is highly decentralized, with some 470 Canada Employment Centres (CECs), 187 itinerant service units and employment offices in 100 post-secondary institutions, providing services in employment and unemployment insurance. National headquarters and a regional office in each province co-ordinate and support the activities of the CECs.

24.9 This chapter represents the second year of our value-for-money audit of the Unemployment Insurance Account. In our 1988 Report, Chapter 18, we reported the results of our audit on the following activities:

- UI claims processing;
- administration of the Records of Employment;
- placement services; and
- integration of employment and unemployment insurance services.

24.10 This year's chapter focusses on four activities, namely:

- investigation and control services;
- labour market information;
- counselling services; and
- general administration and support services.

24.11 The main objective of the audit was to determine whether these activities had been managed with due regard for economy and efficiency and whether the UI Act and its regulations had been complied with.

Information for Parliament

Benefits paid for insurance are not separately disclosed from those paid for socio-economic purposes

24.12 The primary purpose of the UI Program is to insure contributors against loss of income for a temporary period of unemployment, during which the claimant must actively seek employment and be available for work.

24.13 The UI Program has evolved over the years into a compulsory and contributory socio-economic program as well as an insurance program. Certain benefits such as those relating to maternity, adoption, illness, training, job creation, and fishing and those pertaining to the regional extended phase are often associated with the socio-economic aspects of the Program. The costs of these benefits are disclosed separately under current legislation, in the Commission's annual report and in Part III of the Main Estimates.

24.14 Much has been said or written about the use of the UI Program to meet socio-economic objectives other than the original insurance objective.

24.15 For example, since the 1971 unemployment insurance reform, seasonal workers receive the same protection as other contributors. These persons must meet the same conditions for eligibility as other claimants and must therefore actively seek "suitable employment" for a "reasonable period" following their loss of work. They must then seek and/or accept another job for which they are qualified, even if the job offers a lower rate of pay. According to CEIC data, benefits paid to seasonal workers are becoming an important part of the total regular benefits paid (30 to 40 percent or nearly $3.6 billion). These are not disclosed separately to Parliament.

24.16 We acknowledge that there is some difficulty in identifying the purpose of a benefit payment, and thus, in distinguishing between the portions related to insurance and to socio-economic aspects of the UI Program. However, separate disclosure of regular benefits paid to various groups of recipients is essential for those financing the program and for sound decision-making by regulators, legislators and parliamentarians.

24.17 Regular benefits paid should be the subject of separate disclosure to Parliament, indicating whether they are related to the insurance or the socio-economic objectives.

Commission's Comment: *We disagree with this recommendation. Full disclosure is already made to Parliament on the various categories of benefits provided under the UI Act. The Act makes no distinction between benefits paid on the basis of insurance versus social objectives, nor does the Act distinguish between seasonal and continuous employment (and workers).*

All UI benefits paid are based on the insurance aspect of the program in that they compensate for a loss of income from employment. It is recognized that UI benefits also have socio-economic effects which are inextricably interwoven with the insurance aspects. The Commission believes that it is not possible to objectively separate these aspects.

Investigation and Control Services

24.18 The Unemployment Insurance Act specifies the criteria for continuing eligibility for regular benefits: claimants must be available for work and must show proof that they are actively seeking employment. Moreover, they must declare all income earned during their benefit period.

24.19 The mandate of Investigation and Control Services (ICS) is to prevent, deter, and detect claim abuses and fraud in programs and services administered under the Unemployment Insurance Act and Regulations. It plays a vital role in the prevention and detection of inappropriate payments by ensuring that benefits are paid only to eligible recipients.

24.20 ICS carried out over one million investigations in 1988-89. From 401,299 investigations that resulted in an exclusion/disqualification, 352,841 cases of overpayment were identified -- 12 percent of the three million claims received. Of these, 173,065 cases involved intentional misrepresentation for which administrative penalties were imposed. Identified overpayments totalled $135 million and penalties imposed amounted to $26 million. Exhibit 24.1 shows the results for the last five years. Operating costs for these services totalled $40 million and involved 950 person-years for 1988-89.

24.21 In the pursuit of its mandate, ICS directs its operations nationally, regionally, and locally. National headquarters is responsible for program, policy and procedures, and for research and development. The regions review and supervise activities related to investigation and control while providing operational guidance at the local level. The CEC is responsible for the operation of investigation and control activities. Investigation and control officers at the local level are responsible for verifying or dispelling any suspicions of improper payments and uncovering facts establishing whether an offense has been committed.

24.22 This year, we examined investigation and control activities in 10 CECs in four provinces (New Brunswick, Quebec, Ontario and Manitoba).

24.23 The objective of ICS is to reduce UI fraud and abuse, in a cost effective manner, while being sensitive to claimants and employers.

Control measures difficult to apply

24.24 During our audit, cases were brought to our attention which illustrate the difficulty in applying controls to ensure continuing eligibility of claimants. Examples include seasonal workers and university students. These cases do not violate the provisions of the UI Act, but it is questionable whether they meet the conditions of availability for work and active job search requirements.

24.25 In our opinion, control measures are difficult to apply in the present context. To safeguard the integrity of the UI Account, sound management can be achieved only through an understanding of the respective roles, and the involvement and goodwill of employers, workers, claimants and CEIC personnel.

Few preventive and deterrent initiatives

24.26 In recent years, the Commission has undertaken initiatives that focussed primarily on the detection activity of ICS. Some of these initiatives involved the use of computer matching to detect undeclared earnings; others related to operational strategy such as the development of a fraud indicator system and a policy on voluntary disclosure by claimants.

24.27 There is some deterrent effect from the current improvement in efforts to detect instances of fraud and abuse. The Commission continues to detect many cases of overpayment each year, representing some 12 percent of the three million claims

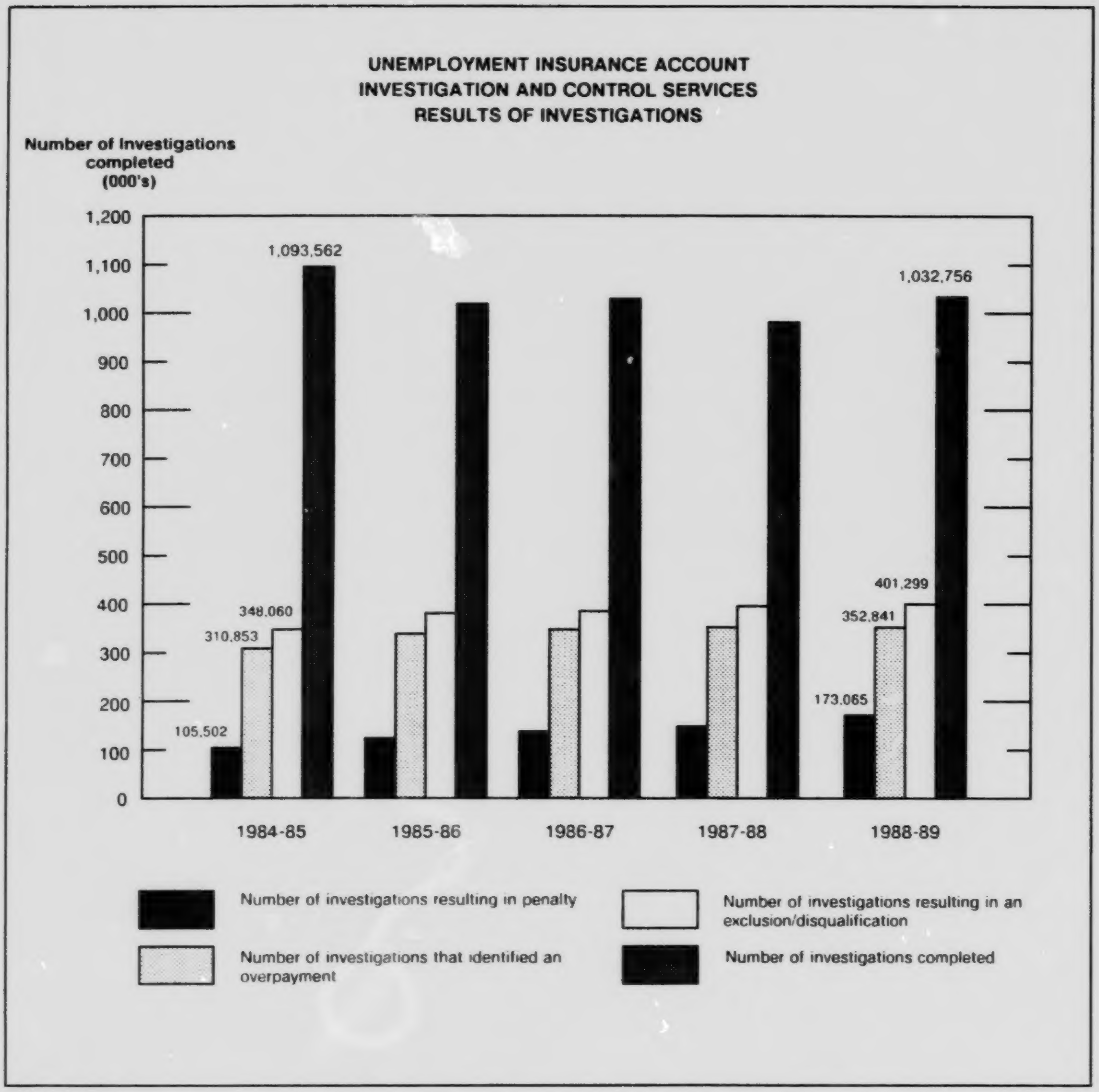


Exhibit 24.1

submitted for benefits. Our audit found that in at least one out of two cases of overpayment, another overpayment had been identified in the two preceding claims of that person. For these claimants, previous detection of undeclared earnings had not been an obvious deterrent. Until recently, few initiatives had been undertaken for purposes of deterrence or prevention.

24.28 The Commission completed a program evaluation of the UI controls during the past year; 90 percent of the employers and claimants surveyed perceived the Commission's control activities as ineffective. It was also noted that only one third of employers and claimants were aware of UI control activities.

24.29 No strategy has been implemented for raising public awareness of the probability of detection and the resulting penalties. Results of investigations are not systematically communicated to the public or advertised. Furthermore, we have noticed almost no reference to Investigation and Control Services in the public areas of local CECs we visited in the past two years. Such visibility could have a significant deterrent effect.

24.30 The Commission should:

- **continue to emphasize and develop preventive measures; and**
- **increase the visibility of its investigation and control function in CECs and to the public.**

Commission's Comment: *We agree with these recommendations. A key to deter and prevent abuse is a reliable detection program coupled with effective information dissemination so that potential abusers are aware that such abuse will be detected.*

The Commission is continually developing new detection programs and refining existing ones. In addition, the Commission on 1 September 1989, has implemented an information strategy which will address the need for greater visibility of its investigation and control function through regular messages to claimants, press releases and the introduction of a control emphasis in all brochures. The Commission is in the process of enhancing the visibility of Investigation and Control in local offices. The Commission believes that the combination of these approaches constitutes an effective prevention program.

Overpayments are not detected, on average, until one year after infractions are committed

24.31 Of the one million investigations done annually by ICS, over 75 percent originated from the results of cross-matching computer files. There are mainly three sources used for cross-matching with benefits paid to identify whether the claimants declared their earnings or employment while receiving UI. These are:

- the Record of Employment (ROE) sent by employers directly to the Commission;
- reports from employers upon hiring personnel; and
- computer pay lists supplied by employers to the Commission.

The late detection of infractions, weak penalties, and non-recovery of overpayments from other federal programs have little deterrent effect.

24.32 Providing the last two sources is optional for employers. The number of employers submitting this information has been relatively stable since 1984 (72,000 for report on hiring and 118 major employers for wage reports). Treasury Board agreed in November 1987 that departments and agencies for which it is the employer will participate in the report on hiring program. Full implementation is expected in 1989-90.

24.33 We examined these detection systems to determine whether they were reliable and whether any serious delays existed in detecting overpayments, which could impact on their timely collection.

24.34 A sample of 227 completed investigations revealed that overpayments were detected by these systems, on average, one year after the infractions were committed by claimants. Furthermore, for 20 percent of investigations originating from computer matching of ROEs, it would have been possible to detect an overpayment some 10 weeks earlier, when the claimant filed a new claim. Such earlier detection would reduce the delay in recovering overpayments.

24.35 The Commission should detect any previous overpayments at the time claimants file a subsequent claim.

Commission's Comment: *The Commission agrees but, at the present time, such an initiative based on available (manual) systems would delay benefit payments to all new claimants. However, the Commission will undertake to study the technological feasibility of instituting a computerized means of implementing the recommendation which would be cost effective and which would not reduce service to claimants.*

Low and inconsistent application of penalties

24.36 The UI Act permits a penalty up to a maximum of 300 percent of the weekly benefit rate (average rate for 1988, $203). We noted that the level of penalty ranged from 25 percent to 75 percent, but was normally 50 percent of the weekly benefit rate. However, in one province it was only 40 percent. Furthermore, at the time of our audit the level of penalty established was no different for first-time and repeat offenders. This leads to weak and inconsistent application of penalties.

24.37 The Commission's program evaluation had also concluded that 75 percent of employers and claimants believed that deterrence could be improved by imposing heavier penalties or by implementing stricter controls.

24.38 The Commission should ensure that penalties are applied on a consistent basis, taking into account whether the claimant is a first-time or repeat offender.

Commission's Comment: *We agree with this recommendation. A new penalty policy for claimants has been implemented on 1 September, 1989, under which the schedule of penalties per offence is as follows:*

- *100 percent of the weekly benefit rate for first-time offenders;*
- *200 percent of the weekly benefit rate for second-time offenders; and,*
- *300 percent of the weekly benefit rate for all other offenders, i.e. the maximum penalty amount permitted by the Unemployment Insurance Act.*

No interest charged on overdue accounts and failure to recover overpayments in other federal programs

24.39 The benefit overpayments and penalties receivable represented $140 million at 31 December 1988. We noted that the UI Act does not allow the Commission to charge interest on overdue accounts, a practice which would encourage reimbursement.

24.40 Although the Commission recovers overpayments from its own programs and from salaries paid to federal government employees, the opportunity exists to also recover overpayments from money owed to claimants by other federal government programs (i.e. Revenue Taxation) before the account is written off. We noted that over $27.4 million in overpayments has been written off in the last five years.

24.41 The Commission should pursue further opportunities to recoup overpayments from other amounts owing to the claimant by the government in other programs.

Commission's Comment: *Under the legislation for set-offs, the approval of other federal departments is required. We are working with the Office of the Comptroller General to pursue further agreements.*

Incompleteness of information on Record of Employment leads to unnecessary investigations

24.42 Approximately 50 percent of the completed investigations that originated from the cross-matching of computer files did not end in identifying overpayments. However, it had still been necessary in all cases to confirm the number of applicable weeks to earnings reported on Records of Employment (ROE) and/or reasons for voluntarily leaving employment. If employers were requested to provide this information on their ROEs, the number of investigations could be reduced significantly, thus reducing the time and effort required of both the Commission and the employers. Compliance with such a requirement would be easier under the new computerized ROE system.

24.43 The management of the Canada Employment Centres we visited advocated that all the necessary information be required initially on the ROEs to avoid having to ask the employer for the information referred to above. We noted that one employer enters on all ROEs the pay dates corresponding to each week of insurable earnings, to minimize the Commission's requests for additional information. We support such an initiative.

24.44 The Commission should ensure that the new computerized Record of Employment provides all the information required for control purposes.

Commission's Comment: *We agree in principle, and will pursue the intent with the private sector.*

Shortcomings in the sharing of responsibilities

24.45 Activities related to benefit control, including various interview programs, are shared by the Insurance Services and the ICS. Insurance officers are responsible for decisions on overpayments, non-entitlements, disqualifications and penalties, but only upon the recommendation of investigation and control staff.

24.46 Our audit found shortcomings in the sharing of these responsibilities and decision processes, which weaken accountability and affect the timeliness of decisions. First, there are delays of approximately one month in recording decisions once investigations have been completed. Second, in five to ten percent of cases, representing approximately $10 million, insurance officers overturn their own decisions without consulting further with investigation and control staff. Moreover, these cases are not being reported to management.

24.47 The Commission should clarify responsibilities for the decision process between Insurance Services and Investigation and Control Services to ensure timely recording and reporting of decisions to management.

Commission's Comment: *We agree with this recommendation. Pilot projects are presently under development to speed up the decision making and recording process. The Commission will continue to maintain the impartiality inherent in a separation of duties between the investigation officer and the adjudiction officer. Moreover, steps will be taken* *to make management aware that 5 to 10 percent of insurance officer decisions are changed based on new facts being presented by claimants.*

National Employment Services

Introduction

24.48 In our 1988 Report (paragraph 18.50 to 18.107), we examined the placement services offered at Canada Employment Centres. In this year's audit of National Employment Services we focus on Labour Market Information and Labour Market Adjustment Services. Together these activities account for $165 million, of which 88 percent is recovered from the UI Account (see Exhibit 24.2).

24.49 The mandate for National Employment Services under the Unemployment Insurance Act is to "assist workers to find suitable employment and employers to find suitable workers".

24.50 In 1988-89, NES was subject to a comprehensive internal program evaluation. In response to this evaluation and to the concerns raised in our 1988 Report, the Commission is redefining the mandate of the Employment and Insurance Program in order to strengthen interrelationships between the Employment and the Insurance activities. The practice of decentralizing decision making and delegating as much authority as possible to local managers continued.

Labour Market Information (LMI)

24.51 We audited 11 CEC offices in five provinces, focussing on analyses of local labour market information and the way the information was linked to the local planning strategy, which is the key planning tool for a CEC manager. The manager is responsible for ensuring that:

- local labour market information is used to establish needs and priorities in communities; and
- CEC interventions are strategically planned and controlled to ensure their responsiveness to both Commission and local priorities and needs.

24.52 The analyst is responsible for collecting, organizing, analyzing, and disseminating local labour market information. The timely provision of this information is essential to the operation of placement services, to the insurance program, and to the selection of training programs offered.

24.53 In an efficient labour market, jobs to be filled are matched as soon as possible to workers qualified to fill them. A CEC should be able to quickly inform its worker clients about relevant job openings and its employer clients about the availability of suitable workers. As CECs have "revitalized" and developed a self-service labour exchange, the availability of appropriate and easily accessible information has become increasingly critical to the success of the service.

24.54 CEIC plays an increasingly important role in long-term labour market adjustments. CECs administer programs and services designed to help workers increase their employability and to help employers adjust to changing technologies and conditions of international competition. This is especially important in the wake of the adjustments required as a result of the free-trade agreement.

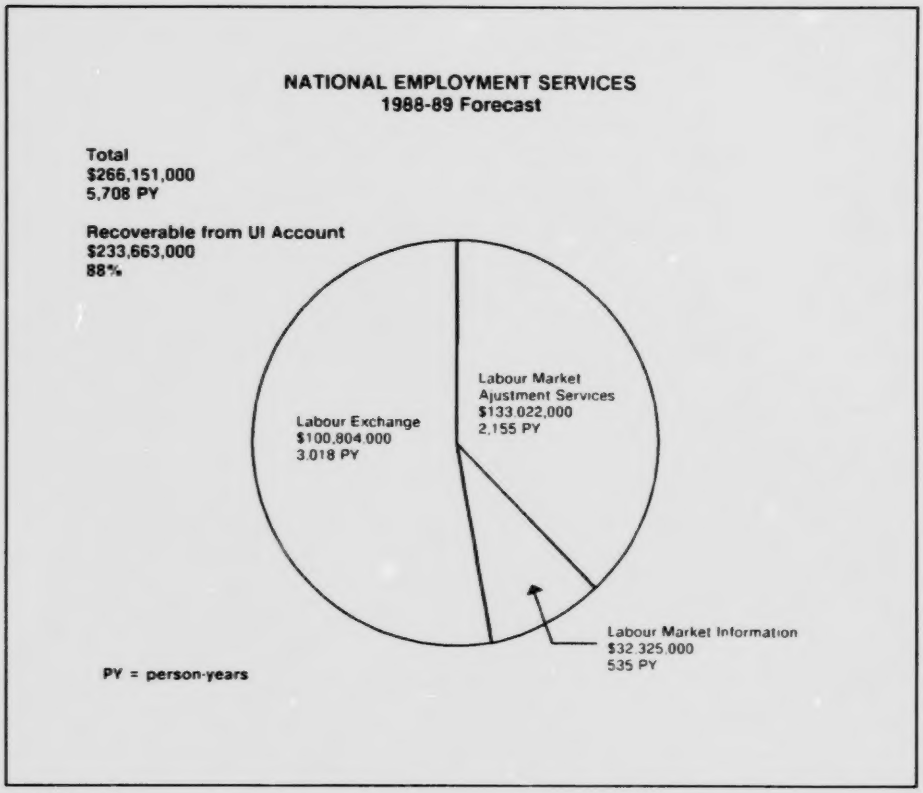


Exhibit 24.2

24.55 As CEIC delegates more responsibility to CEC managers for decisions on funding Canadian Jobs Strategy projects or training programs, the need increases for relevant analysis of local labour market information. We examined the degree to which such information is incorporated into the local planning strategy. However, we did not examine whether this led to appropriate funding decisions on local Canadian Jobs Strategy training projects.

Preference for data collection over analysis

Local labour market analysis usually provides useful short term information but too often is not sufficiently linked to local planning strategies.

24.56 Most CECs have information that could help CEIC in the short term to meet its labour exchange role in the local labour market and to serve the control and investigation needs of the Insurance Program.

24.57 Only a few CECs use longer-term or structural analyses of occupational and unemployment trends and consult with providers and users of local labour market information to identify present and eventual gaps between supply and demand. In other CECs, we observed a preference for data collection over analysis to support local planning strategies.

24.58 We observed insufficient linkages of labour market information to local planning strategies, making it difficult for CEC managers to set priorities among possible local training projects. This could result in the wasteful allocation of training resources.

24.59 The Commission should ensure that appropriate emphasis is placed on analysis of local labour market information.

Commission's Comment: *The Commission will give greater emphasis to the analysis of local labour market information (LMI) to support the development of local planning strategies and the effective delivery of programs and services. During the 1990-91 fiscal year, additional resources and computer support will be allocated to this activity. The Commission will also review and update the training programs for analysts and will be addressing the training needs of CEC managers during the next two years.*

Differences in regional implementation may impact on the economy and efficiency of the LMI activity

24.60 Within an overall national policy for local labour market information, each region has adopted its own approach to implementation. We found that the activity could function adequately with relatively few resources; however, we observed considerable variations in the development of the local LMI function. For instance:

- In the five regions visited, there were four different software packages for processing and reporting local labour market information. The fifth region had not yet provided computers or specially designed regional software to most labour market information analysts.
- In Toronto, two district level analysts served the entire metropolitan area, while in Montreal there were eight analysts at the local level alone.

24.61 As a result of a decentralized approach to implementation, the CECs we visited had no standards for timeliness, pertinence, reliability, and accessibility of the labour market information produced. CEIC does not know whether such differences in regional implementation impact on the cost-effectiveness of these activities.

24.62 The Commission should:

- **monitor the achievements of CECs that have developed an adequate labour market information function;**
- **encourage other CECs to emulate successful approaches; and**
- **develop and monitor standards to ensure uniformity and quality of local labour market information analysis.**

Commission's Comment: *Field tests will be undertaken in the fall of 1989 to examine new methods of presenting labour market information (LMI). A performance monitoring system will be tested concurrently in the same sites. Test results will serve to determine the feasibility of establishing national standards for the type and quality of labour market information products and for the analysis required in their production. Analysis of test results will be completed by 31 March 1990.*

The Commission will continue to encourage and support networking activities among its local analysts and their Regional LMI Coordinators so that expertise and innovative ideas may be shared. The feasibility of establishing a national clearing house for information on LMI products and analytical techniques will be studied prior to 31 March 1990.

Counselling Services to Workers

Introduction

24.63 Labour Market Adjustment Services offers a variety of programs and services at CECs to workers and employers. One of its objectives is to reduce the duration of unemployment and to increase the employability of new entrants and those returning to the labour force. Our audit focussed on counselling services to workers and followed up on our 1983 and 1988 recommendations to implement performance measures.

24.64 The major service is employment counselling for workers who are identified as not "job-ready". About 1,800 CEC counsellors reported that they spent about half their time (nearly 877 person-years) on counselling workers in 1988-89.

24.65 Depending on the situation and the geographic region, counselling services to workers offer:

- referrals to training programs in the Canadian Jobs Strategy;
- assistance in becoming job-ready so that they can search for work independently;
- referrals to language training; and
- marketing of those with special difficulties.

Counselling services are more accessible in some CECs than others

24.66 Counselling serves as a screen or gateway to other CEIC programs. Access is determined by a short interview to determine the client's service needs. About 20 percent of workers who are interviewed receive a referral to counselling. Most other workers are referred to the self-service job information centre.

24.67 CEIC operational guidelines state that, wherever possible, there should be a maximum of 10 working days (two weeks) between the interview to determine the service needs and the initial counselling interview. The average wait at the 10 CECs we visited was 9.5 days, but at two of them the average wait was about one month. A delay in the case of someone receiving unemployment insurance could increase the costs to the UI Fund by prolonging the period during which benefits are being paid. As noted in paragraph 77, the CEIC did not measure, or report to senior management, the timeliness of counselling service.

24.68 In the CECs we visited, management expected a counsellor's full day to range from five to nine counselling interviews, or the equivalent time in contacts with clients. CEIC's program evaluation of counselling observed that "working with five or more clients represents a full day's work".

24.69 However, counsellors in the CECs we visited averaged less than four interviews per day. At the typical scheduled length of 45 minutes per interview, this is three hours of actual counselling per day. Even with an allowance for time spent on documenting files, conducting sessions on creative job search techniques, learning about local labour market and training opportunities, liaising with other local institutions and marketing clients to employers, it would appear from the information available that many counsellors have time to conduct more interviews. However, the structure of the time reporting system does not give management precise information about counsellors' overall productivity.

24.70 Another reason for the apparently low volume of interviews is that some clients do not attend their appointments. Although most counsellors schedule at least five interviews per day, we found that 25 percent of counselling appointments were cancelled and not rescheduled, or the client failed to report. In most CECs this extra time was spent only occasionally with "walk-in" clients.

24.71 Since individual counselling is expensive, it may not always be the most appropriate way to help workers enter or return to the work force. CEIC has developed alternatives and supplements to individual counselling, including group information sessions, job finding clubs, sessions on creative job search techniques, and group counselling. CEIC has not assessed the cost effectiveness of most of these alternatives.

24.72 We found only one CEC that offered a job finding club, one offering group counselling, and three offering sessions on creative job search techniques. There was no obvious rationale as to why some CECs and not others offered alternatives to individual counselling.

24.73 The Commission should assess the cost effectiveness of alternatives to individual counselling and, where warranted, ensure that Canada Employment Centres offer them.

Commission's Comment: *The Commission regards cost as only one factor in deciding to implement group approaches to employment counselling. The Commission is encouraging CECs to implement alternatives to individual counselling such as Group Employment Counselling, Job Search Strategies Sessions and Job Finding Clubs. It is also examining the extent to which the delivery of specific employment counselling group services could be delivered by external contractors in a cost effective manner.*

Cost effectiveness indicators will be developed for group and individual counselling methods. These will be based on outcomes information obtained through follow-up. These measures will be tested during 1990-91 and if assessed as being useful in managing the performance of the service will be adapted in 1991-92.

Counsellors do not report UI claimants to Insurance Services when they fail to report for an interview

24.74 In our 1988 Report (paragraph 18.110), we stated that CEIC did not have an effective system for dealing with UI claimants who failed to report to an employer for a job interview. This year we are concerned about UI claimants who do not attend scheduled appointments with counsellors.

24.75 In most CECs visited, Employment Services did not provide information to Insurance Services on claimants who failed to report to counselling interviews without good cause. The Commission's employment manual sets out policies regarding the provision of claimant information to Insurance Services. Since claimants may not be fulfilling conditions of entitlement to UI benefits, it is important that Employment Services communicate these cases to Insurance Services in order to preserve the integrity of the UI Program.

24.76 The Commission should ensure that counsellors adhere to CEIC policy and inform Insurance Services when UI claimants fail to report, without good cause, for an interview.

Commission's Comment: *By 31 March 1990, the Commission will revise its guidelines on the referral to Insurance Services of claimants who fail to report, without good cause, for counselling interviews. New performance measures are being proposed for 1990-91* *which will capture the number of referrals from Employment Services to Insurance Services.*

Senior management still lacks regular information on the performance of counselling

24.77 In our 1983 Report (paragraph 8.113), we observed that CEIC attached more importance to the counselling process than to the results and that there was no monitoring of cost and quality of service. In the follow-up chapter (paragraph 14.225) of our 1985 Report, we reported that a project to measure the effectiveness of services to individuals had begun. As of June 1989, little progress has been made.

24.78 In 1988-89, the Commission implemented surveys at the local level to measure the quality of service to workers, but results have not been rolled up to regional or national headquarters. Although we commend CEIC for its commitment to improving quality of service, we found that these surveys do not measure such factors as speed and effectiveness of individual assistance, as originally intended, but only client satisfaction with the overall services provided at the CECs. We believe it is an elaborate and unnecessarily costly means of seeking client feedback, considering its limited usefulness to CEC managers.

24.79 Recently, some productivity indicators were selected for use in 1989-1990. However, there is still no follow-up on counselling cases to obtain useful performance information on the quality or effectiveness of counselling services. We believe that follow-up would also improve the counselling process by demonstrating to clients CEIC's interest in whether they have followed through on plans agreed to with counsellors. According to the Commission, approximately 33 percent of counselling cases were referred to Canadian Jobs Strategy (Human Resource Development) training programs. Follow-up is done under these programs, but results are not segregated to provide feedback on cases referred by counselling services.

24.80 The Commission should:

- **fully implement performance measures for counselling services;**
- **institute follow-up to the counselling process;**
- **link to follow-up results of other CEIC programs, where applicable, in order to minimize duplication; and**
- **adopt less costly means of seeking feedback on client satisfaction with service and ensure that results are reported to management.**

Commission's Comment: *A working group will be established to research and develop recommendations for performance measures related to employment counselling, including outcome measures through client follow-up. Testing of proposed measures will begin in April 1990 with implementation of approved measures in fiscal year 1991-92.*

Immediate steps will be taken to study the potential application of the Canadian Jobs Strategy follow-up survey in providing the required follow-up data to establish the relationship between employment counselling, success in CJS programs and subsequent employment.

The Commission's approach to surveying quality of service contains only one question dealing with client satisfaction. The Commission is taking action to improve the cost-effectiveness of the current system through improvements to the computer support system *and to the analysis of results. These improvements will be introduced prior to 31 March 1990.*

The Commission regards the current survey instrument as a local management tool and does not intend to consolidate local office results for use at the regional or national levels.

Some outreach projects are poorly linked to CEC activities

24.81 Through some 300 contracts with public and private non-profit agencies, National Employment Services provide additional counselling and placement services to specific underserved target groups and remote localities. The cost is projected at $24 million for 1988-89. A typical program might offer counselling to women in an urban area; another might serve natives on a reserve; others might focus on assisting handicapped persons. Most Outreach projects have been in operation more than five years; about 25 percent have been active for more than ten years. According to CEIC, about 800 full-time employees offered 270,000 counselling interviews in 1988-89. This compares with 460,000 counselling interviews at CECs.

24.82 From our audit of nine of these projects we concluded that Outreach projects are not usually linked to the local planning strategies of CECs, because decisions on the selection of projects are made at the regional level. Services offered by CECs, particularly since revitalization of Employment Services, sometimes overlap with Outreach projects as well as with services offered by provincial and/or local organizations.

24.83 The Commission should ensure that planning and selection of individual Outreach projects are better linked to the local planning strategies of CECs.

Commission's Comment: *Regions and CECs have been directed to regard Outreach as an integral component of the local planning strategy. The provision of Outreach services must be linked through the local planning strategy to Canadian Jobs Strategy programs as many Outreach clients are prime candidates for such program assistance. CECs are responsible to ensure co-ordination and co-operation with Outreach projects so that projects can fulfill their contractual obligations.*

At the national level, the Commission is examining ways to further integrate Outreach and the Canadian Jobs Strategy.

General Administration and Support Services Costs

Definition

24.84 Section 117 of the Unemployment Insurance Act specifies that the cost of administering the Act shall be charged to the Unemployment Insurance Account and financed by employer and employee premiums. Since the Canada Employment and Immigration Commission (CEIC) and the Department are administering other programs (Immigration and Human Resource Development Programs), the operating costs are separately identified so that general administration and support services charges, commonly called overhead costs, can be allocated to the UI Account.

24.85 Overhead costs are generally defined as costs that are incurred in support of programs or services but are not readily identifiable with program outputs or services rendered. The administration costs of the UI Account include operating costs, which are directly related to delivering the Insurance and the National Employment Services activities, as well as overhead costs which cannot be directly associated with the delivery of these activities.

24.86 In examining the allocation of overhead costs to the UI Account, we noted that CEIC has not defined them clearly, including the identification of the specific administrative services and costs that comprise them. Without a clear definition, it is difficult for CEIC to assess and monitor actual overhead costs chargeable to the UI Account and to compare the overhead costs of individual regions.

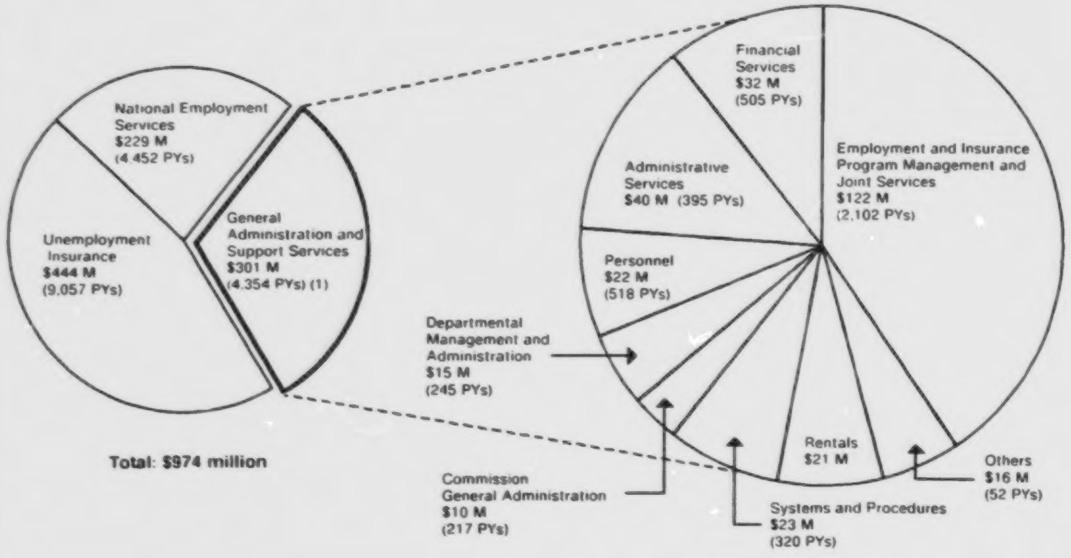
24.87 Thus, in our analysis of overhead costs we included the costs of Corporate and Special Services and Program Management and Joint Services for CEIC, but excluded overhead costs for the Insurance and National Employment Services activities of regional offices and at headquarters. The major components, representing $375 million and 5,502 person-years, are as follows:

- Corporate and Special Services ($222 million and 3,033 person-years forecast for 1988-89):
  - Finance;
  - Administration;
  - Personnel;
  - Strategic Policy and Planning;
  - Public Affairs;
  - Internal Audit; and
  - Rental of office space (only the portion related to general administration and support services).
- Program Management and Joint Services ($153 million and 2,469 person-years forecast for 1988-89):
  - Line management (at regional headquarters, district offices and local offices);
  - Support services (at district and local offices);
  - Program management (at national and regional headquarters, including management personnel and their immediate staff); and
  - General office reception (at local offices).

General administration and support services represent 31 percent of the total administrative costs of the UI Account

24.88 For 1988-89, the overhead costs chargeable to the UI Account amounted to $301 million or 31 percent of the total cost ($974 million). The overhead costs are charged to the UI Account on a pro-rata basis according to a formula approved by the Treasury Board. Exhibit 24.3 shows the breakdown of these costs and person-years by key activities.

24.89 We compared the overhead cost per UI claim for the last six years. The total cost per claim remained relatively constant during that period. The overhead portion of the cost per claim decreased slightly but was still important ($93 per claim) when compared to the cost of delivering the Insurance Services ($137 per claim) and the National Employment Services ($71 per claim) for a total of $301 in 1988-89.



ADMINISTRATION COSTS
Charged to the Unemployment Insurance Account
1988-89 (Forecast)

(1) Equivalent person-years (PYs) of the cost chargeable to UI

Exhibit 24.3

Potential savings could be achieved

24.90 We compared the full costs of general administration and support services per UI claim, by region, including National Headquarters (NHQ) costs. The overhead costs varied from $83 to $145 as follows:

	Number of UI claims (1988)	Overhead costs per claim		
		Regional	NHQ	Total
Newfoundland	141,690	$ 52	$ 32	$ 84
Nova Scotia	132,680	66	41	107
New Brunswick	129,650	89	56	145
Prince Edward Island	27,970	80	50	130
Quebec	968,060	51	32	83
Ontario	932,480	55	34	89
Manitoba	120,140	85	53	138
Saskatchewan	96,220	82	50	132
Alberta & NWT	268,230	60	37	97
British Columbia & Yukon	413,690	51	32	83
Total	3,230,840	$ 57	$ 36	$ 93

24.91 As indicated in the above table, the variation in overhead cost per claim is 75 percent. In the absence of any established targets, such a variation indicates the need for further investigation to determine where potential savings could be achieved.

24.92 Employment and Immigration Canada should:

- **clearly define overhead costs and their components and ensure their consistent reporting by each region; and**

- **establish a reasonable target for overhead costs with a view to controlling and further reducing costs.**

Employment and Immigration Canada's Response: *The EIC reporting system (EIIS) produces detailed information reports on all activities, responsibility centres and objects of expenditure within the Commission. This provides Senior Management with the facility to assess costs and identify areas for potential savings. EIC does not see the advantage in grouping such costs into a composite overhead definition. EIC will continue to review the various components of what the Auditor General refers to as overhead with a view towards further cost reduction wherever possible.*

25

FOLLOW-UP TO THE FINANCIAL MANAGEMENT AND CONTROL STUDY OF 1987

25

FOLLOW-UP TO THE FINANCIAL MANAGEMENT AND CONTROL STUDY OF 1987

Main Points

25.1 The agencies of the Treasury Board are encouraging departments to make improvements to their systems for financial management and control. They have yet to assess the extent of change as the result of their recent initiatives (paragraphs 25.10 to 25.56).

25.2 The initiative to increase ministerial authority and accountability (IMAA) has been moving forward. Progress in terms of signed agreements has been slower than first anticipated, but more are coming. We cannot comment on the end results until cost and performance information systems are further developed, more annual management reports are submitted, and accountability reviews take place. However, we remain concerned about accountability (25.14 to 25.34).

25.3 In general, departments have initiated action on the observations and recommendations of the 1987 Financial Management and Control Study. Slow improvement is indicated in some important areas and problems are recurring. Leadership is still required from central agencies to improve financial management, and departments need to be vigilant in applying internal controls (25.57 to 25.78).

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FOLLOW-UP TO THE FINANCIAL MANAGEMENT AND CONTROL STUDY OF 1987

Introduction

The Financial Management and Control Study (FMCS)

25.4 In 1987 the Office reported the results of its two-year study of financial management and control in departments and agencies. Chapter 4 of the 1987 Report to the House of Commons contains the full text of our findings and recommendations.

25.5 **What the 1987 study found.** After examining nine departments, the study concluded that there were significant deficiencies in financial management. It recommended improvement to systems for financial management and accountability and strengthening of the way resources are allocated and departmental operations are controlled. The study reported significant improvements in basic financial controls since our initial FMCS in 1975 but observed that problems still existed.

25.6 FMCS made recommendations to departments and to central agencies -- the Treasury Board Secretariat and the Office of the Comptroller General. Each department formally responded to the recommendations made to it. The central agencies did not disagree with the study and later responded during the proceedings of the Standing Committee for the Public Accounts (PAC).

25.7 **After the 1987 study was published.** Six departments and the central agencies appeared as witnesses before the PAC. Central agencies outlined initiatives to deal with the concerns raised in the study. Based on the hearings and information presented, the PAC made a report to the House of Commons in June 1988 giving further commentary and making specific recommendations to the government. The government had not tabled a response to this report prior to dissolution of the 33rd Parliament.

25.8 With a view to achieving productivity improvements, one suggestion the PAC made was that the government instruct all departments to implement productivity measurement plans and to report progress by 31 March 1989. We are informed that central agencies did not agree with this particular recommendation.

25.9 **Follow-up scope and approach.** In view of the study findings and the increasing pressure for departments to manage resources cost-effectively, we conducted a follow-up from November 1988 to April 1989 but have also considered information provided to us subsequent to this period. We approached it in three ways. First, we reviewed activities of central agencies; we focussed on the progress of the initiative called Increased Ministerial Authority and Accountability (IMAA) and on the activities of the Office of the Comptroller General. Second, we re-visited eight of the original study departments. Thirdly, we analyzed the results of our ongoing audits in terms of financial management and control issues. The result of our follow-up is reported under two headings: Activity at the Centre and Progress of Departments.

Activity at the Centre

The agencies of the Treasury Board are encouraging departments to make improvement to their systems for financial management and control. They have yet to assess the extent of change as the result of their recent initiatives.

Response to FMCS

25.10 Starting where the study ended. Given the extent of deficiencies, FMCS raised questions about the role of central agencies. These were:

- How can sound resource allocation take place without reliable information on costs, efficiency and effectiveness of operations?
- What is the dividing line between "letting the managers manage" and ensuring that departments are managed so as to meet the objectives set by government ?
- What is the centre's role in the delivery of financial information systems?
- What mechanisms exist at the centre to detect problems in departments, and what can and should be done when problems are identified?

25.11 Central agencies' response. Central agencies have communicated to us responses to the above questions; they involve complex issues and interrelationships. These questions and answers relate more to reporting and accountability after resources are given to departments than to the processes that go on before resource allocation. We have abbreviated their answers to present the essence of the approach being taken by central agencies.

- A complex and evolutionary process exists for making resource allocation decisions in an environment of fiscal constraint. While operational planning frameworks are of key importance, reliance also is, or will be, placed on many other systems for information. These include IMAA documents, internal audit and program evaluation reports, Part III Estimates, annual reports of departments, and ongoing communications with senior line managers and financial managers in departments. It was never expected that most results could be aggregated up to the level of program objectives; however, emphasis will continue on the need for performance indicators.
- Reliance will be placed on reports and accountability reviews under IMAA, as well as the other sources of information outlined above, to assess whether government objectives are met.
- Departments are responsible for their financial systems, while the central agencies set standards and best practices for departments to follow, provide advice, and monitor sources of information for compliance.
- Monitoring and advising departments would be facilitated through the information sources mentioned above, as well as audit and evaluation reports, special studies, and exchange of information and advice through such means as the Interdepartmental Financial Management Advisory Committee of senior full-time

financial officers. The central agencies would intervene in problems only as necessary. Departments are primarily responsible for corrective action.

25.12 IMAA, other initiatives, and ongoing work were considered to be a way of responding to the FMCS findings and recommendations. These were seen as essentially matters of compliance with existing requirements. Central agencies did not draw up a new plan of action but have considered the FMCS results in the course of their work. Similarly, central agencies did not establish a mechanism dedicated to monitoring, assessing or causing departments to take specific corrective action in response to FMCS recommendations.

25.13 **Our follow-up considered this response.** We reviewed the activities of the central agencies, taking into account their response. Exhibit 25.1 gives a basic summary of the results of our follow-up as related to FMCS recommendations directed specifically to the Treasury Board Secretariat and the Office of the Comptroller General. The remainder of this section elaborates on what we found.

Increased Ministerial Authority and Accountability (IMAA)

25.14 In June 1986 the Treasury Board introduced the IMAA concept following its decision in February 1986. This announced a change in the Board's approach to decision-making which, when fully implemented, would significantly increase the authority and accountability of departments and agencies. It has been described by the central agencies as a fundamental change in philosophy that could significantly alter the relationship with departments and the management culture of the federal government. This is being done gradually and we are informed that it might take from 5 to 10 years. It involves reduction of administrative requirements and authority changes for all departments, as well as increasing delegation of authority to specific departments. Departments are invited, on a voluntary basis, to sign a memorandum of understanding (MOU) under IMAA, which is a three-year agreement between a department and the Board involving submission by departments of an annual management report, and a formal accountability review at the conclusion of the MOU.

25.15 Since 1986 the central agencies have devoted much effort to implementing the IMAA concept on a government-wide and a department-by-department basis.

IMAA and planning frameworks were at a critical point of beginning to gain momentum.

25.16 During our follow-up we noted that milestones or targets were not available as reference points from which to measure or predict the progress of IMAA and the transition in financial management and control. While much has been done, we could not say how results to date compare with what was planned or intended.

25.17 The progress of IMAA appears to have been slower than first anticipated. Three years have passed, with 3 of the approximately 30 major departments having signed an agreement to March 1989. These three account for about 8 percent of the total program expenditures of the federal government. As of May 1989, three more agreements had been signed, for a total of six, and we were told that seven more are well advanced. The first two annual reports were sent to the Treasury Board in 1988. The first accountability reviews are scheduled for spring 1990, the final year of the initial agreements.

25.18 However, numbers should not be considered as the sole criteria for judging the progress of IMAA.

FOLLOW-UP TO THE 1987 FINANCIAL MANAGEMENT AND CONTROL STUDY
SYNOPSIS OF ACTIVITIES IN CENTRAL AGENCIES
AT 31 MARCH 1989

Precis of Study Findings and Recommendations	Activities of the Treasury Board Secretariat and the Office of the Comptroller General
There is a lack of accountability between departments and the Treasury Board. A recent initiative, "Increased Ministerial Authority and Accountability" (IMAA), is designed to fill this gap.	IMAA continues as a priority. Guidance material is available. Many departments are in the discussion phase: six have reached negotiation, three have signed agreements. Two annual management reports have been submitted; there have been no accountability reviews.
Treasury Board should re-examine the policy for operational plan frameworks and, in conjunction with departments, clarify objectives, produce meaningful performance measurements and link results with resources.	The policy has been revised in draft. Work continues toward clarifying objectives and measures of performance. A guide to costing outputs was issued in 1989.
The Office of the Comptroller General should monitor the development of efficiency measurement systems.	There is no evidence of monitoring; this recommendation was not accepted.
Performance information in Part III Estimates should be improved and initiatives reported on a comparable basis.	Instructions calling for improvements have been issued. A process to review all Part IIIs is working.
Office of the Comptroller General should issue directives and guidelines for cost-effective control.	Useful guidance materials have been issued. Work plans list many projects, some important ones outstanding.
The need for annual reports by departments should be re-examined. If continued, standards are needed for their content.	Statute revisions are proposed to allow choice (subject to conditions) to discontinue annual reports. Standards have not been issued.

Central agencies are working to improve financial management and control. They have yet to obtain sufficient information to know the effect of initiatives on the financial management and control practices of departments and agencies. Several important measures are to be undertaken or completed.

Exhibit 25.1

25.19 An important result of the process is that dialogue has opened up between central agencies and departments, and information on IMAA is now widely available. Up to March 1989, 21 departments had entered into discussions with the Treasury Board Secretariat, with 6 having progressed to signing an MOU by May 1989 and others entering final stages of negotiation. An IMAA Handbook has been prepared, a progress report has been issued by the Board, and guidelines for the preparation of departmental reports have recently been drafted.

25.20 IMAA is to increase departmental authority. Increased delegation of authority is intended to provide greater flexibility in resource management and administration, and to reduce the involvement of central agencies. Authority will flow outward to departments, while the amount of reporting to central agencies will be reduced. This includes decreasing or removing constraints that have existed for some time and eliminating or reducing requirements for information on resource planning. IMAA is not intended as a vehicle for creating authority or returning it to the Treasury Board.

25.21 The shift in authorities. According to Treasury Board data, as of October 1988 some 114 authority changes had been proposed by six departments. Of these, 87 were submitted for Treasury Board approval and 36 were approved. Examples of those approved are: authority to set terms and conditions of grants and contributions; authority to use non-salary moneys to pay for part-time employees; ability to retain any internally generated savings; and ability to provide for multi-year resourcing. As other MOUs are signed, more delegations will be approved.

25.22 According to July 1989 data of the Board, 72 percent of authority proposals (for the six departments which have signed an MOU) were approved in whole or in part. This ratio includes items relating to government-wide policy reviews of the Board. Approved proposals were in the following areas:

- delegation of certain departmental operations to the regional level;
- job classification authority below the management level;
- travel, conferences and memberships;
- language training and development; and
- increased limits for contracting.

25.23 The process of reviewing requests for authority changes has resulted in both departments and the Secretariat learning more about authorities and the need for change. This is beneficial in itself, in terms of achieving better understanding. We were informed that some proposals were withdrawn because sufficient authority was found to exist, other ways were found to overcome a constraint, an existing requirement was misunderstood in its application, or an authority requirement had already been changed. Consultation between the Board and departments apparently reduced the number of unworkable proposals.

25.24 It was not our purpose to determine which authority changes should or should not take place. Because of the few departments that have negotiated MOUs, and the number and nature of authority changes approved so far, we did not see an extensive shift in delegation of authority for financial management and control. A gradual approach is being taken so that a balance is maintained between authority and accountability, and central agencies can meet their responsibilities while providing greater freedom for departments.

Streamlining administration and relieving paper burden

25.25 In conjunction with authority delegation, the Treasury Board has been amending information and administrative policies as one way to increase productivity in administration.

25.26 When IMAA was announced in 1986 it was accompanied by measures for relaxing administrative requirements. These included increasing departmental limits for competitive contracts and eliminating the need for Board approval in certain administrative areas.

25.27 Reporting requirements have also been reduced. For example, departments need only submit information technology plans every three years instead of annually, multi-year human resource plans are to be provided every three years under IMAA with updates through an annual management report, and multi-year operating plans need not be updated as frequently. Further elimination of reporting requirements and directives is pending. In April 1989, the Board agreed to delete a further six reporting requirements and 174 directives.

25.28 We noted that submissions by departments to the Treasury Board for funding and other approvals continued to decline in number by about 23 percent over the past two years. A new Treasury Board submissions guide was distributed in draft form to all departments in June 1989.

25.29 The Board has also improved management guidance to departments by publishing the first edition of the "managers desk book", to communicate the essential elements of Treasury Board policies. The Board also intends to review all policies and rationalize them into a single series of manuals by 1991.

A concern for accountability

25.30 A primary aim of IMAA is to achieve increased accountability and to encourage productivity improvements. Two departments have submitted annual management reports so far. No department has yet undergone an accountability review. The first is scheduled for early 1990, when the first three-year MOUs are to be completed.

25.31 An MOU under IMAA involves parties agreeing on resource levels and the circumstances under which these might change. Attachments to the agreements feature accountability frameworks that set quantitative performance targets in some areas but in others only outline generic standards or expectations. MOUs do not incorporate specific economy or efficiency gains to be met by departments, although they include some performance measurements relating to efficiency and effectiveness. There is no central policy for economy or efficiency goals, which is consistent with the centre's view about productivity measurement plans as indicated in paragraph 25.8. If productivity is to be encouraged through MOUs, we are uncertain how it will work. It will be left to departments, with encouragement from the centre, including the possibility of retaining resources associated with any internally generated efficiencies.

25.32 Outside the IMAA process, however, departments make resource reductions as part of the constraint policy administered by the Board. According to information released by the Treasury Board, the five-year "downsizing" plan for the public service has produced a net reduction of 11,596 authorized person-years since 1985 (about 5 percent) across all departments and agencies. Other Board data show a net real reduction in annual salary and operating budgets of departments and agencies of approximately $369 million (5.7 percent) when 1987-88 is compared to 1984-85.

25.33 The three MOUs signed under IMAA contain a common understanding that adequate planning, monitoring, control, internal audit and program evaluation systems will be in place, or that an agreement will be reached to put them in place. They recognize that department officials and Treasury Board officers should work closely together to ensure that these systems are maintained and enhanced. And they recognize the need to identify and implement improved performance indicators. This is important, in view of the fact that our follow-up in departments concludes that meaningful cost and performance measurement data have yet to become a working reality. As noted in many studies going back to the 1970s, such information is important not only for the success of initiatives such as IMAA but also for better financial management and control within departments and for oversight by Parliament.

25.34 With respect to accountability, in our view IMAA is at a critical point. Further developments and experience in this area will come in future with the submission and review of reports, which will focus ministerial attention on the delivery of programs and Board policies. Based on this experience there will be a need for central agencies to:

- consider where information should be expanded, eliminated, or focussed in annual management reports and performance reviews, consistent with ministerial accountability and the role of central agencies in this regard;
- know whether departmental systems and practices are providing the relevant performance information in a reliable and timely manner; and
- obtain information for assessing whether the anticipated productivity improvements in administrative functions are being achieved, without significant risks to the safeguarding of assets and their efficient use.

Operational Planning Frameworks of departments have been improving

25.35 Operational Planning Frameworks (OPFs) are essential to the IMAA process. They are equally important to financial management and control in departments and for reporting to Parliament.

25.36 As recommended by the 1987 FMCS, the policy for OPFs has been revised. At 31 March 1989 a draft was ready for inclusion in Chapter 5 of the Policy and Expenditure Management System Manual.

25.37 The Office of the Comptroller General has assessed the frameworks of 24 departments over the past two years on behalf of the Treasury Board Secretariat and IMAA. At the time of our follow-up, a documented summary of the results of the assessments was not available. However, we understand that an analysis of departmental OPFs formed the basis for the policy revision now in draft form.

25.38 Assessment of planning frameworks has been based on the judgment of Treasury Board officers and an OPF review panel. While no doubt this has helped to improve OPFs, the fact that there were no common assessment criteria or summary analysis prevents us from commenting on the consistency or completeness of this work. Without duplicating these assessments or conducting a detailed file review, we cannot report whether, on the whole, the objectives of programs are actually now sufficiently clear, multiple accountability has been appropriately defined, and resource use is related to results achieved where it is possible to do so. Generation of summary analysis of this type was not considered important by central agencies, given the specific focus on the OPF of each department and the uniqueness of each of these frameworks. In future audits we will assess the implementation of OPFs and the new policy when it is issued in final form.

25.39 We were told that the quality of frameworks ranged from some requiring extensive revision to others needing only minor modification. It is still common to find few meaningful performance indicators being generated. Further improvements in form and content might be possible if specific guidance were given to departments to augment the revised OPF policy. This could include where to avoid costly information gathering that produces data of only incremental value.

25.40 For more than five years, much effort on the part of many people has gone into the creation and development of OPFs. The task now is to make them work as an integral part of managing programs and accountability.

Conclusion

25.41 IMAA has been moving forward. However, we found that progress in terms of signed agreements was slower than anticipated, and the full benefits of IMAA may not be realized for some years to come. Both IMAA and planning frameworks were at a critical point of beginning to gain momentum in their implementation and achievement of accountability. Increased delegation of authority and accountability for individual departments under an MOU has, so far, been limited to a few but others are coming. We cannot comment on the end results until more annual management reports are submitted in accordance with guidelines, and accountability reviews take place.

25.42 We plan to review IMAA again, particularly as agreements are completed or renewed in each department. Their contribution to financial management and control will be assessed in each case.

The Office of the Comptroller General

25.43 The Office of the Comptroller General (OCG) is one of two entities serving the Treasury Board; the other is the Secretariat. The Comptroller General reports to the President of the Treasury Board and has the rank and power of a deputy head of a department. The Comptroller General also has a functional relationship to the Secretary of the Treasury Board in areas of joint interest such as OPFs.

25.44 We note that the responsibilities of the Comptroller General, as communicated in 1978 by the President of the Treasury Board, have not been updated by means of a formal Board policy and delegation of authority. Orders in Council have appointed succeeding Comptrollers General but have not been used as a means of defining OCG authority and accountability pursuant to the Financial Administration Act. Nonetheless, there is common understanding and reconfirmation of the role and responsibilities of the OCG through the annual submission of its Estimates and testimony before the Public Accounts Committee.

25.45 While the Part III submissions are not themselves authority documents, they serve to communicate the responsibilities of the Comptroller General and his Office. They have implied authority since they have been tabled by successive Presidents of the Treasury Board. The program objective of the OCG is currently stated as:

> to see to the establishment and maintenance of sound management practices in the federal government.
>
> developing policies and standards.....and promoting and monitoring improvements in the practice of financial and operational management, in departments and agencies.

25.46 The OCG has gone through a number of changes since July 1987. A new Comptroller General was appointed in June 1988. New directions have been taken, and the OCG has been reorganized. Closer working relations with the Treasury Board Secretariat have been developed, with the Comptroller General becoming an ex-officio member of the Secretariat's Executive Committee and his Office providing assistance for IMAA and supporting the policy centres of the Treasury Board. The basic mandate of the OCG has not changed; however, its activities and structure have changed in the following ways:

- It no longer addresses broad management practices, but has begun to focus on financial management and controls, including the strengthening of internal audit and program evaluation functions.
- A new branch was created in 1988 dedicated to financial management information and related systems.
- The Management Practices Branch was replaced by the Audit and Review Branch, with increased emphasis to be given to audit activities across government, in particular the preparation of an annual Government Internal Audit Plan to provide feedback to other policy centres.

25.47 With the end of the Improvement in Management Practices and Control (IMPAC) program and the elimination of the Management Practices Branch that was involved in it, the OCG intends to re-emphasize the monitoring activity of remaining branches.

25.48 The OCG has issued new and revised materials for information and guidance (see photograph), including common criteria for evaluating financial systems, working standards for program evaluation, a guide to costing outputs, and the first government consolidation of the internal audit plans of departments. It has also served on departmental committees for system implementation, consulted with departments on the acquisition of ready-made software for financial systems and participated in groups made up of user departments.

25.49 In the 1975 FMCS and again in 1987, concerns were expressed about financial information systems. This included the lack of integration of financial and operating data, duplication of system development and data entry, and the lack of useful information. While the initiatives taken by the OCG have merit, their desired result seems to be delayed. There are some continuing problems related to data utility, poor project management, cost overruns and duplication of effort. These are reported further in paragraphs 25.73 and 25.74.

25.50 **Streamlining financial controls.** A number of projects to make financial controls more cost-effective are either in process or are planned for the future. For example, starting in 1989-90 the use of statistical sampling is to be encouraged for verifying accounts before making a payment. The initiative is intended to guide the level of work required, to improve the prevention or detection of errors and, in conjunction with other controls, to ensure adherence to Treasury Board payment regulations. This is only one of some 70 ongoing projects of the Accounting and Costing Policy Branch dealing with basic financial functions such as methods of payment, cash flows and forecasting, banking arrangements, revenue and receivable control and accounting.

25.51 Looking to the long term, the OCG issued a draft strategy in April 1989 for creating a new financial information and accounting infrastructure for all of government for the 1990s. This followed its 1987 survey to determine the financial information central agencies need to discharge their responsibilities, including IMAA.

25.52 The survey collected the views of senior officials about the kinds of information that were needed but not available. Some of those were: consolidated expenditure data on common functions, summary financial data on special initiatives and asset holdings, more

Guide to the Costing of Outputs in the Government of Canada
INTERNAL AUDIT
PUBLICATIONS

Central agencies continue to provide guidance materials to departments as part of their role in strengthening internal audit and program evaluation functions. (see paragraph 25.48)

timely information for performance monitoring and variance analysis, and expenditure information by economic or target groups. At present, these kinds of information are not readily available to central agencies or Parliament. They would be useful for identifying opportunities for economy and efficiency gains, improved financial management decision making, and enhancing the understanding of government spending. However, they have a cost.

25.53 If the strategy is approved, it could significantly influence the role of the Treasury Board Secretariat and the Office of the Comptroller General. It will be a major strategic initiative, with a series of main stages and supporting projects requiring effective project management and the upgrading of departmental capabilities. Improved capacity for financial information management will be important, judging by the deficiencies we have reported in departmental systems. Reliable cost figures for the project will not be available until priorities are established, system specifications have been defined, and the effects of upgrading or replacing systems are known, including the central accounting system of government. Total incremental costs have only been roughly estimated by the OCG at this stage; it expects more accurate numbers when it completes an impact analysis. The OCG indicates that some $600 million is now spent each year in financial information systems for departments and agencies of the federal government.

25.54 Meanwhile, work in a number of important areas is to be completed in the shorter term. For example:

- An operational planning guide for departments is now scheduled for March 1990. This is to provide a reference document for managers on how to plan and budget in different types of operations.

- A system for drawing on internal audits as an information source for monitoring and feedback to various policy groups of the Treasury Board is being developed, but is not yet complete. The internal audit function is to be assessed by the OCG for reliance by both central agencies and departmental management.

- An inventory of financial systems, now two years old, is to be updated. (We noted that there had been little direct involvement or monitoring of the implementation of new financial systems.) Study of the quality of financial information is already under way.

- The OCG intends to reassess financial function requirements and to develop common indicators for measuring performance results.

25.55 The OCG recognizes the need to develop and co-ordinate ways of anticipating financial management and control requirements, assessing the performance of the financial function, and acting on problems in a timely manner. If this is done, it should better answer the question relating to monitoring and the detection of problems in paragraph 25.10, as recommended by the 1987 FMCS.

Summary Conclusion

25.56 Central agencies have taken a number of initiatives to improve financial management and control. However, they do not yet have sufficient information to determine the impact of these initiatives. There are several important measures to be undertaken or completed.

Progress of Departments

In general, departments have initiated action on the observations and recommendations of the 1987 Financial Management and Control Study. Slow improvement is indicated in some important areas and problems are recurring. Leadership is still required from central agencies to improve financial management, and departments need to be vigilant in applying internal controls.

25.57 Exhibit 25.2 shows the progress on the main conclusions of the 1987 FMCS as they were considered to apply across all departments. Overall, this indicates reasonable progress to date in about half of the issues that we have been able to assess. The progress of each department included in the study and follow-up is reported in paragraphs 25.58 to 25.68.

25.58 Variable results. As might be expected, improvements in complex areas are taking the most time. Progress has been slower in resource planning and budgeting, cost-benefit analysis, and the implementation of costing and performance measurement systems.

25.59 Progress, or lack of it, varies from department to department and from subject to subject. This is apparent in the following paragraphs that summarize the results of follow-up in each department. More detail about most of these is provided in Chapter 26. The follow-up for the Department of Supply and Services is reported at more length in Chapter 21.

25.60 The Department of Agriculture has made progress in revising its planning framework and performance indicators, strengthening the role of the financial function, establishing a process to improve the management of information resources, reducing long outstanding accounts receivable, and introducing a new financial information system on or close to budget and ahead of schedule. These represent a considerable advancement in financial

FOLLOW-UP TO THE 1987 FINANCIAL MANAGEMENT AND CONTROL STUDY
PROGRESS ON MAIN CONCLUSIONS OF THE STUDY

Conclusions of the 1987 Study	Number of Applicable Departments	Departments Indicating		
		Progress	Little Progress	Too Early to Assess
Resource Decision and Control				
Departments should ensure that needs, costs and benefits of initiatives are fully considered and documented.	7	1	4	2
Mechanisms should be improved to clarify objectives, measure performance and link financial requirements to expected results.	8	2	4	2
Information for Managing				
The management of information systems was found to be significantly deficient. Discipline is needed from systems development through to project control.	7	5	2	0
Departments should know what cost information they require and get it.	6	2	1	3
Reliable efficiency measurement systems should exist where operations lend themselves. Operating data should be integrated with financial data.	7	3	3	1
Internal Controls				
Internal control weaknesses that have been identified should be corrected, in particular to ensure that assets are safeguarded.	6	2	3	1
The role of financial officers should be reviewed.	4	3	1	0
Accountability				
Performance information to Parliament should be improved, and initiatives in Part III Estimates reported on a comparable basis.	5	2	1	2
Appraisal of managerial performance should include the use of resources in relation to results achieved.	3	0	1	2
		20	20	

While there are indications of progress, significant areas are taking time to show results, and problems continue to arise. For a number of items, the work of a department is at too preliminary a stage. Progress will be assessed in the future.

Exhibit 25.2

management and control. However, improvements to inventory and capital assets management were not substantially advanced at the time of our follow-up.

25.61 A planning framework is being implemented, with performance indicators to support planning, budgeting, and accountability. However, these indicators are not yet being systematically produced. This is to begin in 1989-90. Similarly, combining operational and financial information for analysis and performance assessment is a challenge for the Department of Agriculture in the future.

25.62 The Department of Supply and Services has commenced actions to improve productivity, most of which are in process. This involves strategic planning and the use of technology to do the work at less cost. The Department is evaluating alternative ways of delivering services, developing a new Public Service Compensation System at a cost of $55 million that is expected to reduce annual operating costs by up to $23 million, and continuing to rationalize and apply technology in computer operations where staff have been reduced by 65. It also intends to replace cheques with electronic payments direct to the banks of program recipients. It is implementing a new system that measures the performance of regions, and is beginning to report the full cost of its service lines. However, it is too early to determine the impact on the management of operations and controlling of costs. We did not expect immediate resolution of some of the more significant productivity issues reported in 1987; this will take time. However, progress has been made.

Progress or lack of it, varies from department to department and from subject to subject.

25.63 In Employment and Immigration we observed in 1987 that formal analysis had not been done of the probable financial effects of alternative approaches for the Canadian Jobs Strategy program. We also reported some weaknesses in the systems for financial management and control. Satisfactory progress has been made in the area of financial information systems. However, no policy on financial analysis for new programs has been put in place. Little progress has been made in the area of information for resource allocation and operations for the Canadian Jobs Strategy and the National Employment Service.

25.64 At Energy Mines and Resources, progress was satisfactory in financial management at the branch level, financial controls and management of the informatics function. Some progress has been made in corporate level information; however, we could not conclude that corporate management critically challenges the Department's resource base each year. There are still inconsistencies in the quality of information for planning, managing and reporting on new initiatives. The financial control system for accountability for assets needs revision.

25.65 External Affairs' progress in implementing major changes to processes and systems, which address concerns raised by us in 1987, has been slow. There are delays in the multi-million dollar COSICS on-line secure information and communication system, in the implementation of the FINEX financial accounting system -- particularly at posts abroad -- and in improvements to planning and monitoring of post operations and the PERNET personnel information system. Managing real properties abroad, and simplifying the Foreign Service Directives are other areas in which improved processes and systems have not been fully implemented. We remain concerned that the Internal Audit Division has not fulfilled its comprehensive audit mandate and that there have been few significant studies that measure the effectiveness of External Affairs program activities listed in Part III of the Estimates.

25.66 National Revenue - Customs and Excise has addressed most of the recommendations made in our 1987 Report. However, certain issues have not been fully resolved. The financial function is now playing a stronger role, and steps have been taken to improve the quality of financial analysis to support initiatives. Work has been undertaken to update the departmental accountability regime, including a revised operational planning framework. Some new program performance indicators have been developed and implemented; and program effectiveness indicators and qualitative performance indicators on the effects of facilitation initiatives and level of service are continuing to be developed and refined.

25.67 The Department of Veterans Affairs has enhanced the role of the financial function in resource allocation and budget preparation, and has improved financial controls. However, the new financial information system cannot, as yet, be relied on for management information or preparation of year-end accounts. The existing departmental reporting system had to be run in parallel longer than anticipated.

25.68 Transport Canada has made only limited progress in meeting the deadlines it established for implementing the major initiatives reported to Parliament as important to improving financial management and control (see Exhibit 25.3). Implementation of half of the initiatives has been delayed, in some cases by over three years. We were informed that the original target dates were overly optimistic and did not reflect the complexities, the necessary policy changes or the availability of resources. At present, it is not possible to assess the validity of the new target dates. We will have to follow this up again.

25.69 A continuing need for better financial management and control is illustrated by our audits since 1987. In our 1988 Report we identified various opportunities for better resource management, and in 1989, we continue to report items of concern related to financial management and control such as lack of cost analysis and information to guide resource allocation.

25.70 In addition to matters contained in our annual reports, analysis of our ongoing financial audits reveals that there are still deficiencies in basic functions such as recording, payment processing, compliance with authorities, reconciliations and the protection of assets. The items shown in Exhibit 25.4 came to our attention as we carried out audit tests primarily designed to reach an opinion on financial statements. The incidences reported in the exhibit should not be used to estimate the overall error or control deficiencies in financial systems across government. While these data are not sufficient to conclude on the adequacy of internal controls as a whole, the type and frequency of errors suggest that diligence is required in applying them. This need is demonstrated by the observations that follow.

Deficiencies in inventory management and control

25.71 Our 1987 audit of the materiel support system of the Department of National Defence reported, among other things, a number of deficiencies in the management of inventories. The Department is taking action on most of our recommendations. In a few cases, factors external to the Department constrain its ability to move as quickly as it would like in making needed changes. Given the longer-term nature of most of the departmental initiatives, such as the new Canadian Forces Supply System that will not be operational until the late 1990s, it is important that interim measures be taken so that problems do not persist until the major initiatives are completed. The Department has undertaken a number of initiatives of this type, although resources constrain the pace at which they can be pursued. It is important that these efforts be maintained and enhanced.

25.72 Inventory management and control are also of concern to the OCG. A government-wide study conducted on its behalf reported some unnecessarily high levels of materiel inventories. The study noted that inventory control was seriously deficient; there was a lack of policy and standards, purchasing and stocking practices were costly, record keeping was

DEPARTMENT OF TRANSPORT
FMCS II FOLLOW-UP

Department's Initiative in Response to Observations and Recommendations	Original Target	Revised Target	Comments
Assess performance indicators for aids to navigation and waterways development in Marine, develop indicators for the Aviation Group and the financial function.	Dec. 1987	Marine - Complete Aviation - Complete Finance - Complete	In Aviation, Department reports problems with quality of data resulting in limited initial use. OAG observed implementation problems in Finance.
Develop cost recovery guidelines and policies for Airports, Aviation and Marine.	June 1988	Aviation, Airport - Fall 1990 Marine - 1991	Department reports delays caused by complexity of issues, requiring additional inter-departmental discussions, and approvals within the Department
Implement procedures for review and challenge of capital projects and re-allocation proposals.	Sept. 1987	Complete	
Develop revised policy and definitions for fixed assets.	Dec. 1987	Apr. 1990	Policy issued 1 April 1989 Department reports full implementation is linked with 1990-91 budgets.
Develop and implement an integrated fixed asset accounting system.	Mar. 1988	Oct. 1991	Department reports that revisions to the conceptual design and discussions with users and central agencies took a year longer than anticipated.
Develop new objectives to improve revenue collection performance.	Dec. 1987	Complete	
Develop and implement a computerized billing system.	Dec. 1987	31 Mar. 1990	Department reports that development is linked to the commercial accounting project for major airports.
Implement a system of accrual accounting at major airports.	Apr. 1988	31 Dec. 1989	Department reports that as a result of the new direction to be taken in managing airports in Canada, the scope of the new commercial accounting system is significantly greater than the system that was to be implemented in April 1988. A pilot system at one site is scheduled to be completed in 1989.
Implement a new commercial property management regime.	Oct. 1987	Complete	
Develop a national automated materiel management system.	Sept. 1987	Complete	
Re-examine approach to developing and implementing financial management information systems.		In progress	A major internal review of administrative EDP systems has been completed. As new national systems are developed, they will be audited by the OAG.

Exhibit 25.3

SUMMARY OF INTERNAL CONTROL OBSERVATIONS COMMUNICATED TO DEPARTMENTS AS THE RESULT OF ATTEST AUDITS FOR 1988

Type of Deficiency	Number of Observations	Number of Entities
Accounting mistakes, including incorrect cut-off	52	14
Inadequate control over payment processing	32	12
Non-compliance with authorities	32	12
Insufficient reporting documentation	15	10
Poor reconciliation of accounting data	13	10
Insufficient contract control	8	7
Inadequate control over assets	8	6
Inadequate financial analysis	6	4
Other	12	8

The array and frequency of observations suggest that diligence is required in applying internal controls.

Exhibit 25.4

poor and the full cost of carrying inventories was not recognized. The study concluded that basic action was required before more advanced government practices could be introduced. Studies such as this are positive ways of giving Treasury Board useful information about existing conditions, especially where concerns have been expressed, and have revealed numerous opportunities to improve policies and practices. We will follow up on the action taken to address the study recommendations.

25.73 Continuing problems in computerized systems. In 1987 we reported a pattern of project failures, cost overruns, poor performance and duplication of effort. Since then, the Advisory Committee on Information Management (ACIM), which reports to the Treasury Board, has taken action. It has recommended substantially improved project management and systems development standards for use by departments. When these are approved and followed, progress can be expected in the management of these complex activities. In the meantime, while some departments have taken corrective action, others are still experiencing the same difficulties that we outlined in 1987. For example:

- Veteran Affairs is significantly behind schedule in fully implementing its new financial information system. The existing system will have to run in parallel for another year since the new system cannot, as yet, produce financial data that management has confidence in.

- As reported in Chapter 26, External Affairs is incurring considerable cost increases for its new secure information and communication system.

- Our review of controls over selected systems development projects in the Department of Supply and Services revealed that while general guidance for project management was in place, procedures to implement them were still under development.

- In several entities we found that reconciliations between departmental systems and the central accounts of Canada were incomplete or delayed (see Chapter 4, Audit Notes, paragraphs 4.110 to 4.116), raising the possibility of incomplete or unreliable financial information.

25.74 We believe these difficulties can be traced to some common problems that the central agencies could address. For example, many departments did not perform a full feasibility study, preferring to accept studies of alternatives already performed for other departments and on the understanding that the OCG had sanctioned or would be sanctioning the systems purchased. This created some confusion including ambiguous functional specifications and inaccurate forecasts of the computer resources required. Another condition that may have contributed to these problems was the lack of policies or systems for charging the costs of information to the users. Such a practice might create a stronger discipline in information management.

25.75 **Performance appraisals and training.** In 1987 we commented that performance in the areas of financial management and control were seldom reflected in the appraisals of program managers and that minimal training was provided. Our follow-up to the audit of the Management Category reveals that there is no clear perceived connection between the systems of performance appraisal and the granting of pay for performance. Therefore, it is necessary to look to other mechanisms for encouraging changes in management attitudes and practices. The Treasury Board Secretariat is currently reviewing the performance appraisal and pay for performance policy.

25.76 Follow-up at the Public Service Commission indicates that progress has been made in the training available for financial management.

25.77 **In summary.** On the basis of the results of this follow-up, we conclude that departments have responded positively to the 1987 Study. This is encouraging. However, progress has been uneven, and improvements in many areas have yet to be completed. Leadership is still required from central agencies to improve financial management, and departments need to be vigilant in applying internal controls.

25.78 We will examine the financial management and control practices of departments as part of the Office's ongoing audits. We will also conduct in-depth examinations from time to time that focus on specific areas such as financial information systems, cost recovery, non-tax revenues and receivables, inventory management, and financial practices in contracting.

26

FOLLOW-UP OF RECOMMENDATIONS IN PREVIOUS REPORTS

26

FOLLOW-UP OF RECOMMENDATIONS IN PREVIOUS REPORTS

Main Points

26.1 The follow-up chapter reports on the actions taken by departments and agencies in response to our past observations and recommendations. We give a mixed report card. In some cases considerable progress has been made, while in others it has been slow.

26.2 1986 Audit: In three of the four program areas in the **Department of Agriculture** that were audited in 1986 ,reasonable progress has been made. The fourth -- Farm Income Services -- is presently the subject of a major policy review (paragraphs 26.16 to 26.21).

26.3 1987 Audits: **National Revenue - Customs and Excise** has addressed most of our recommendations; however, some issues have not been fully resolved (26.22 to 26.32).

26.4 Action has been taken at the **Department of Energy, Mines and Resources** on a number of problems identified in our report. But major challenges remain. Continuing problems involve inadequate information at the corporate level and for planning, managing and reporting on new initiatives (26.33 to 26.39).

26.5 Progress has been slow in implementing major changes to processes and systems needed to address the concerns identified in our audit of common administrative systems at the **Department of External Affairs**. The Department states that factors beyond its control within the federal government have contributed to delays (26.40 to 26.68).

26.6 The **Department of National Defence** is taking action on most of our recommendations. Many of the initiatives are longer-term and it is important that interim measures be pursued and enhanced. The Department has assisted the follow-up by submitting to us semi-annual reports on progress (26.69 to 26.83).

26.7 Satisfactory progress has been made by **Canada Employment and Immigration Commission** in the area of financial information systems. But no policy on financial analysis for new programs has been put in place. Little progress has been made in two other areas (26.84 to 26.101).

26.8 Our follow-up of **Special Audits** finds that progress has been satisfactory in **Risk Management**. Progress has been made in the use and management of **Microcomputers**. We are going to audit again in 1991(26.102 to 26.112).

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FOLLOW-UP OF RECOMMENDATIONS IN PREVIOUS REPORTS

Introduction

26.9 This is the fifth year that we have reported on the status of action taken by departments and agencies in response to the Office's observations and recommendations.

26.10 We found that the progress in taking corrective action varied among departments. In some cases considerable progress has been made, while in others it has been slow. However, we believe this follow-up work, which generally occurs two years after the original reporting in the annual report, has been useful in keeping the Public Accounts Committee and Parliament informed about action taken to correct the deficiencies noted.

26.11 Follow-up results on Emergency Preparedness (Special Audits Chapter) and Department of Supply and Services audits are contained in Chapters 27 and 21 respectively of this report.

26.12 The follow-up audit on the 1987 Financial Management and Control Study is reported in Chapter 25.

This chapter reflects the status of action taken by departments and agencies in response to the Office of the Auditor General's observations and recommendations.

26.13 Because the findings in the follow-up of the 1987 Management Category Chapter were extensive and wide-ranging, these have also been reported separately -- in Chapter 8.

26.14 A follow-up report on the 1987 Department of National Defence audit of Major Capital Projects has been deferred because the area is included in audit work currently under way and scheduled for reporting in 1991.

26.15 The follow-up of the 1987 National Health and Welfare audit has been deferred to 1990, when the areas covered in the 1987 chapter will be the focus of our audit activity in that Department.

Department of Agriculture - 1986, Chapter 8

Background

26.16 The 1986 audit of the Department of Agriculture reported on a number of diverse program areas:

- Farm Income Services, including Crop Insurance and Western Grain Stabilization, which administers payments designed to protect farm assets in the short run.
- The Research Branch, including the management of its research operations, major capital projects and human resources. The Branch is responsible for maintaining and improving the productivity of the agri-food sector through developing and transferring new knowledge and technology.
- Prairie Farm Rehabilitation programs addressing rural water development, community pastures, and emergency drought assistance for livestock and crops.

- The management, handling, storing and disposing of toxic waste and hazardous materials from laboratories and research facilities.

26.17 The 1986 Report made recommendations in each of these program areas. It was discussed at two sessions of the Public Accounts Committee in April 1987. The Committee was concerned with the Department's slow progress in implementing recommendations from our 1982 audit, as well as its response to our 1986 audit, and asked the Department for a report on its progress, as of 31 December 1987, in implementing our recommendations. The Department of Agriculture submitted the progress report; because its target date for completing many of our 1986 recommendations was October 1988, we scheduled our follow-up audit for 1989.

26.18 Our purpose was to determine whether the Department's efforts in implementing our 1986 recommendations represent reasonable progress and are consistent with commitments made to the Public Accounts Committee. We did not attempt to evaluate the success of the Department's efforts in correcting the problems we identified in 1986.

26.19 Our follow-up findings are based on a management representation we requested from the Deputy Minister of Agriculture outlining the Department's actions to December 1988 in respect of each of our 1986 recommendations. We verified this by examining the documentary evidence cited by the Department in support of its statements of progress, and we conducted limited interviews with program managers.

Conclusion

26.20 Based on our review of the Department's management representations to us, except for progress in the Farm Income Services area as described in the following paragraph, we believe there has been reasonable progress overall in implementing our 1986 recommendations. Progress in some areas has not been as rapid as the Department originally anticipated in its responses to the Public Accounts Committee. However, the Department has indicated that this slippage is due, in no small part, to the scope and complexity of the tasks involved.

26.21 In the Farm Income Services area, while significant progress has been made, many of the structural problems related to our recommendations remained unresolved at the time of our follow-up. However, a major policy review, encompassing all the programs in this area, is in progress. This review was initiated by the Minister, and its terms of reference include virtually all the areas of concern with respect to these programs raised in our chapter. The final resolution of these matters awaits the results and recommendations of the policy review, to be presented to the Minister.

Department of National Revenue - Customs and Excise - 1987, Chapter 5

Background

26.22 Our 1987 audit of the Department of National Revenue - Customs and Excise was part of the government-wide study of financial management and control. We audited the revenue systems and the planning, budgeting and reporting framework, including a review of the financial and internal audit functions and the Memorandum of Understanding with Treasury Board. We also reviewed two financial information systems and the remission programs.

Conclusion

26.23 The Department has addressed most of the recommendations made in our 1987 Report. However, some issues in certain areas have not been fully resolved. Three of our recommendations on remission programs were directed to the Department of Finance and the Department of National Revenue - Customs and Excise. Significant improvements have also been noted in some of these areas.

Observations

26.24 Operational Plan Framework. The Department, the Treasury Board Secretariat and the Office of the Comptroller General have been working together to update the Departmental Accountability Regime which includes a revised Operational Plan Framework. This document has been approved by the Secretariat and the framework component has been formally approved by the Treasury Board. The Department has included new program performance indicators which will provide more meaningful information to Parliament, senior management and the central agencies. Some of these indicators have been developed and implemented; for example, indicators relating to revenue, accounts receivable, tax change and percentage of accounts audited in the Excise Branch. Program effectiveness indicators and qualitative performance indicators on the effects of facilitation initiatives and level of service are continuing to be developed and refined.

26.25 Financial function. The financial function is now playing a stronger role at Customs and Excise. Some examples of this are an improved performance measurement framework in the Departmental Accountability Regime, improved information in Part III of the Estimates and a new Project Manager's Handbook.

26.26 Managing initiatives. The Department has taken steps to improve the quality of financial analysis to support initiatives. The new Project Manager's Handbook, issued in early 1989, includes improved guidelines on preparing feasibility studies and cost benefit analyses. We have not had an opportunity to review the financial analysis for initiatives prepared since the Handbook was issued.

26.27 Internal audit. Internal audit has strengthened its activities in the areas of audit planning and computer auditing. The Internal Audit Long Range Plan is now structured according to the Operational Plan Framework. The number of audits of computer systems has increased. The Department has started to strengthen the computer auditing capability through staffing and training and is continuing its efforts in this area.

26.28 Information to Parliament on remission programs. The government has taken steps to improve the information Parliament receives on remission programs, but there is still little information available on the results that have been achieved. Semi-annual reports on new remission orders and details on all remission orders over $20 million are now required to be tabled in Parliament. The reporting of remission orders in the Public Accounts was revamped. Starting with the 1988-89 Public Accounts, departments will report remissions at the Order-in-Council level rather than reporting those in excess of $1,000 by beneficiary. National Revenue - Customs and Excise has included some information on remissions in its 1989-90 Part III of the Estimates.

26.29 Evaluation of remission programs. The Duties Relief Act, which brought together five major remission programs, was repealed and replaced by sections of the Customs Tariff proclaimed in January 1988. The Department of Finance indicated that many other remission orders will be eliminated as a result of the Free Trade Agreement between Canada and the United States. As a result, it is the Department's view that remission programs have been or will be terminated; that the value of tariff remissions will be reduced from $1 billion to $50 million-$100 million annually by 1998; and that further cuts in this annual total will be made by continuing to convert remissions into statutory provisions. The Department of Finance advised us that since its evaluation resources are limited, it intends to use these resources to examine other tax measures of a continuing nature and greater significance. In our opinion, although many of the remission programs form part of the Customs Tariff, remissions such as those relating to the machinery program and other remission orders should continue to be evaluated from time to time to ensure that they are achieving the results expected of them.

26.30 Cumbersome remission process. The government has streamlined the tariff relief process. Section 101 of the new Customs Tariff authorizes the Governor in Council, on the recommendation of the Minister of Finance or the Minister of National Revenue, to remit taxes by order. There is no longer a need for the President of the Treasury Board to recommend the remission. The Department of National Revenue - Customs and Excise has informed us that it is developing internal procedures for using its Legislative Index System to improve the efficiency and effectiveness of processing Orders-in-Council.

26.31 In the April 1989 federal budget, the Minister of Finance announced the conversion of several long-standing remission orders to statutory provisions. The Budget Papers stated that the conversion will provide the business community with greater certainty regarding tariff relief and will relieve the administrative burden which the remission orders place on the importing community.

26.32 Special temporary entry remissions. Regulations were drafted by the Department of National Revenue - Customs and Excise and published in the Canada Gazette on 4 February 1989 with respect to special temporary entry remissions. The Department has informed us that the regulations are expected to eliminate the need for more than 80 percent of the special Orders-in-Council pertaining to temporary entry.

Department of Energy, Mines and Resources - 1987, Chapter 7

Background

26.33 At the Public Accounts Committee hearing in 1988, the Department indicated that it had taken action to address our report. We found that many significant managerial and organizational changes are under way in Energy Mines and Resources. However, the Department has not developed a plan for implementing the specific recommendations in our report, nor monitored progress toward achieving improvements. Although action was taken to correct a number of problems listed as specific examples in our report, major challenges remain.

26.34 Our 1987 audit focused on six main issues. We followed up five of these issues this year. We will follow up on information in the Estimates, Part III, next year.

Progress was satisfactory in three areas:

- financial management at the branch level;
- financial controls; and
- management of the informatics function.

However, there was little progress in two areas. These will require further follow-up:

- inadequate information at the corporate level; and

- inadequate information for planning new initiatives.

26.35 Some progress regarding corporate level information has been made since 1987, notably the signing of a Memorandum of Understanding on Increased Ministerial Accountability and Authority in June 1989. However, the accountability accords between the Deputy Minister and the Assistant Deputy Ministers, and other reports provided to the Deputy Minister include few specific targets, measures of efficiency or levels of service. As a result, we could not conclude that corporate management and staff critically challenge the Department's resource base each year.

26.36 The Department has not established guidelines for planning, managing and reporting on new initiatives. There are still inconsistencies in the quality of information for these purposes for two of the initiatives that we reported on in our 1987 Report.

26.37 Processes used to plan, manage and control work at the branch level, which we found to be generally satisfactory, are essentially unchanged since our last audit. However, information collected and reported at the project and branch level should contain more performance information.

26.38 Specific examples of financial control weaknesses cited in our 1987 Report, have been corrected. However, asset valuation and the system for accountability for assets are very much in need of restructuring. As the result of a recent internal audit, materiel management has developed an implementation plan to address weaknesses.

26.39 Information technology services at the corporate level have been reorganized in a single branch. This will help provide a focal point for planning and monitoring information technology in the Department.

Department of External Affairs - 1987, Chapter 8

Background

26.40 Our 1987 audit of the Department of External Affairs examined common administrative services, including the Finance and Administration Branch, Personnel Branch, Corporate Management Bureau, Internal Audit and Program Evaluation, and related functions at posts abroad. We did not examine the organizational structure of the Department within which these services are provided. In this follow-up exercise, conducted mainly from January to March 1989, we discussed with management in Ottawa the steps the Department had taken to implement our recommendations and reviewed the documentation provided to us on the progress it had made since 1987. We also visited two posts to examine progress at that level.

Conclusion

26.41 Progress in implementing major changes to processes and systems which address our concerns has been slow. There are delays in the multi-million dollar COSICS on-line secure information and communication system, in the implementation of the FINEX financial accounting system -- particularly at posts abroad -- and in improvements to planning and monitoring of post operations and the PERNET personnel information system. Managing real properties abroad and simplifying the Foreign Services Directives are other areas in which improved processes and systems have not been fully implemented. Furthermore, there has been a delay in negotiating an Increased Ministerial Authority and Accountability (IMAA) agreement with Treasury Board. We remain concerned that the Internal Audit Division has not fulfilled its comprehensive audit mandate and that there have been few significant studies that measure the effectiveness of External Affairs program activities listed in Part III of the Estimates. The Department stated that factors beyond its control within the federal government have contributed to delays.

Observations

26.42 The Department of External Affairs is responsible for protecting and promoting Canadian interests abroad and ensuring that the domestic policy developments of other government departments are consistent with Canada's international obligations and foreign affairs interests. The Department points out that these responsibilities, together with the impact of decisions of foreign governments, produce an environment of continuing flux in which long-term planning is difficult and priorities must be constantly reordered and resources reallocated. Recent examples quoted by the Department include the decision of the government to decentralize the aid delivery program to missions abroad, the consequences of international terrorism and political and economic repression on the delivery of the immigration program, and the decision of certain foreign governments to relocate their capitals.

Financial Management and Control

26.43 Changes are slow in the planning and control of program delivery. Many of External Affairs' activities are of a policy development nature. However, program delivery in areas such as immigration, trade, consular services and aid is becoming an increasingly significant aspect of operations in Ottawa and missions abroad. We pointed out in 1987 that the planning process for program delivery required improvements such as development of alternative management strategies at the program level, operational plans -- particularly at the post level -- that were precise enough to use in managing operations, and proper monitoring of the implementation of plans. The Department told us that it had been gradually changing the planning process to add these features.

26.44 We found that these changes have been slow. At the time of our follow-up, the Department was planning to introduce an integrated work planning and reporting system within the headquarters and mission operational planning process, with complete implementation expected for reporting in 1991 under the Increased Ministerial Authority and Accountability (IMAA) regime.

26.45 At that time, however, the Department's efforts had not resulted in significantly better operational planning, monitoring or resource allocation processes. Inconsistencies remained in the quality of annual work plans for individual posts for certain activities. Levels of service were not always clearly defined. The Department had been generating substantial data from its various tracking systems and was assessing their usefulness for planning and monitoring operations. Data collection processes appeared to satisfy the requirements of the Treasury Board and other government agencies for more quantitative information on workload. For activities such as consular and trade, the information gathered was not always independently validated for accuracy, completeness and consistency among posts. The budget process largely continued to be based on existing staffing and perceived need, rather than on a less subjective analysis of the range and extent of services that will be provided at posts abroad for such activities. The planning process has not changed significantly despite the growth in available data. We are told that the proposed changes related to the IMAA process will provide a stronger basis for planning and control. The Department's response has been that, to the extent possible, appropriate measures have been taken to improve planning systems to allow the Department to manage its programs better in the unpredictable environment in which it operates. Deadlines established for implementation of improvements have been agreed to by senior management and necessary resources will need to be reallocated to ensure these are achieved.

26.46 Financial information systems are still being implemented. We were concerned that financial information at External Affairs was being produced on three separate systems, posing problems of incompatibility, duplication and lack of aggregation of information. The Department is still in the process of implementing its new computerized financial accounting system (FINEX) in Ottawa and abroad; it is therefore too early to comment on the results. The outputs in the form of reports to management have not been fully designed, and implementation at the posts is dependent on COSICS. As a result, black book systems will continue to be used in Ottawa and the posts until the new system is fully implemented and users develop more confidence in it.

26.47 The method of allocating costs of passport operations has been revised. We recommended in 1987 that the Department ensure that the cost of passport operations at missions was appropriately estimated and recorded in the Passport Revolving Fund. The costing formula has now been revised.

26.48 Information on capital expenditures is better but not complete. We pointed out in 1987 that the information on capital expenditures presented in Part III of the Department's Estimates was not complete and did not provide continuity with information presented in prior years. Although a schedule of distribution of capital expenditures, and continuity with prior years' information have been added to the 1988-89 Estimates, the information is still not complete since only $62.2 million of the $94.8 million budget is explained, and information on minor capital expenditures has not been included.

26.49 Reasonable progress has been made in control over monetary assets. We identified a need for the Department to improve its monitoring and reporting of monetary assets to ensure that records are complete and cash on hand is kept to a minimum. Reasonable progress has been made in controlling working capital advances to missions, medical loans and security deposits as well as preparing a central registry of debentures, as we suggested.

26.50 Control is still needed for surplus materiel. We recommended that the Department ensure that surplus materiel is properly controlled and adequate materiel records are maintained. We continue to be concerned that inventory records at missions are not universally maintained and kept up to date. Practices for ensuring the proper control of surplus materiel at the missions have not significantly changed. For example, it often remains unrecorded and inventory records do not indicate its age, although this is required to support replacement decisions. Procedures are still needed at headquarters for monitoring mission compliance with departmental regulations on disposals.

Real Property

26.51 Roles and responsibilities. We commented in 1987 that the lack of clearly defined and communicated roles and responsibilities was affecting the Department's ability to manage its real properties. We noted instances of weaknesses in the accommodation planning processes, the monitoring of departmental staff quarter accommodation costs, the adherence to staff quarter standards, and the issuing of guidelines on property management to missions. We recommended that the Department clearly define and communicate appropriate roles and responsibilities for planning and monitoring accommodation.

26.52 Progress in this area has also been slow. In March 1989, the Department started a detailed review and evaluation of its management of accommodation, including its long-range capital plan. The scope and objectives of this study address the issues raised in our

1987 Report, including clearer definition and communication of roles and responsibilities for managing real properties abroad. It has not changed its existing delegation of authority pending completion of this study, scheduled for September 1989.

26.53 Management of property abroad is still reactive. We noted in 1987 that management had not been achieving its objective of increasing ownership of accommodation and reducing rental costs abroad. We recommended that the Department further improve its accommodation planning process by ensuring that inputs to the long-range capital program result from systematic review of current holdings, accommodation needs and costs. This situation has not significantly changed. The involvement of missions in the staff accommodation purchasing process has not been significant. We were told that, while the process of determining needs and reviewing holdings of staff accommodation has begun, adequate planning will not be possible until there is an agreed staff quarter profile for each mission.

26.54 The tendency to manage the capital expenditure program on an ad-hoc basis has continued. Information on missions' accommodation needs, to help set priorities, is not substantially better. Priority areas for acquisition of staff accommodation have been identified but have largely not been acted on. Also, life cycle costing and other useful information is still not used when considering the need for new or replacement facilities.

26.55 We recommended that the Department develop better contingency plan arrangements with the Treasury Board to ensure optimal use of funds available for capital projects and obtain authority to use disposal proceeds when acquiring property for the same purpose. We were concerned that weaknesses in the system would result in missed opportunities in acquiring and disposing of property. We were told that procedures have been developed but cannot be implemented until the Increased Ministerial Authority and Accountability (IMAA) process has been approved.

26.56 We recommended that the Department should negotiate standards for staff quarters with the Treasury Board and monitor adherence to them by missions. The Department has reviewed the standards for staff quarters, as we recommended, and, after approval by the Treasury Board, distributed to posts "New Staff Quarter Guidelines and Accommodation Procedures" in August 1988. Procedures for monitoring compliance with these standards will take effect when the missions send all the necessary information requested by headquarters.

26.57 In our 1982 Report, we observed that the Post Property Manual issued in the early 1970s was out of date. By 1985 a new manual had been drafted but not issued. In November 1988, the Department stated that a special review was expected to be completed by February 1989. However, this document is only half finished and completed sections have not been circulated outside the headquarter's property management area for advice, information or concurrence. At the current rate of progress, this important manual will not be available to managers and staff at the posts in the near future. This is now recognized by the Finance and Administration Branch as a priority for 1989-90.

Human Resource Management

26.58 Personnel information system will not be completed until 1990. The importance of people as a significant resource is being re-emphasized by the Deputy Minister. In our 1987 Report we drew attention to the lack of a formal skills identification system in the Department's human resource planning process. The Department promised to rectify this and has included a formal documentation of employee functional skills as part of a new personnel information system (PERNET). However, the design and approval of PERNET have been slow. Recently an officer was assigned to the project, funds were allocated to cover the $2.4 million development cost over the next two years, and data elements were chosen. We were told that the project will not be completed and the system installed on line until 1990. The delay has resulted from the need to ensure compatibility with another computer system in the Department.

26.59 Review of Foreign Service Directives has been postponed. We had many concerns about the Foreign Service Directives, recommending that the Department compare actual costs to the estimated costs resulting from changes to them and determine the reasons for variances. We are now informed that this comparison and review will not be possible until the new financial information system (FINEX) is fully implemented. This has been rescheduled for 1990.

26.60 Our recommendation that the Treasury Board Secretariat regularly evaluate and report the extent to which the Foreign Service Directives achieve their intent was also postponed until the Board Secretariat review in early 1989. Also, we were told that ways to simplify the directives and make them easier to apply have not been examined by the Department due to postponement of participation by the Treasury Board Secretariat until 1989. Simplification of the Foreign Service Directives is viewed by the Deputy Minister as a matter that requires serious attention.

26.61 Procedures for recording leave are being strengthened. Our recommendation to strengthen the procedures for recording and monitoring leave has recently been responded to by the Department. Procedures used in other departments and consultants' advice are being reviewed to identify opportunities and suggestions for improvement.

Telecommunications and Records Management

26.62 Telecommunications system costs have increased. In our 1987 Report we identified a high risk that cost estimates for the Department's new Canadian On-Line Secure Information and Communication System (COSICS) would be exceeded, and cautioned that savings would not be fully realized. The Department subsequently updated its cost estimates; in August 1988, the Treasury Board approved a cost increase from $111 million to $208.6 million for the project.

26.63 The revised estimate of the cost of the COSICS Office Processing System (COPS) exceeded initial estimates by $41 million because there was no detailed user requirements analysis and insufficient traffic projections in the initial proposal. Other cost increases were due to items not included in the original estimates, such as the chancery alarm and reporting system and additional site preparation that was necessary for installing the systems. The contract for development and implementation of Phase 1 of the project was signed in August 1988.

26.64 The risk of further cost increases still exists. Since performance specifications were not included in the contract for the COSICS Automated Message Switching system (CAMS), it may require additional costs as the design progresses. Also, at the time of our follow-up audit the design of the COSICS Automated Text Storage system (CATS) had not been completed, and the final configuration could require additional costs.

26.65 The additional operational requirements could jeopardize a portion of the expected savings in person-years, which in turn could reduce the internal savings of $81 million projected to finance some of the costs. We propose to conduct a full audit of COSICS implementation following the completion of Phase 1 of the project in the United States.

26.66 Records management standards have not been developed. We recommended that the Department develop standards for records management with a view to improving productivity. The results obtained by working groups recently established to deal with the underlying problems in measuring productivity have not yet been documented. Since COSICS implementation is taking longer than anticipated, and the design of the CATS system has yet to be proven, it will take time before appropriate standards can be applied to records management.

Internal Audit and Effectiveness Measurement

26.67 Internal audit is still not comprehensive. A departmental Inspector General with responsibility for internal audit and reviews has recently been appointed. This strengthens the independence of the function from an organizational point of view. However, we continue to be concerned that steps have not been taken to meet the comprehensive internal audit mandate. We were told that this is due to lack of resources which has resulted in slippages in executing plans. Thus, the Internal Audit Division had not audited major program activities, such as political and economic reporting and trade, or been actively involved in examining controls during the development of the FINEX and COSICS systems.

26.68 Effectiveness measurement could be further improved. The Program Evaluation and Resource Review Division spends time and effort on resource reviews, as well as program evaluations. These are necessary corporate activities that include cost-cutting and person-year savings exercises. The Division has completed a few studies that relate to the measurement of the effectiveness of program activities listed in Part III of the Estimates. Others, we are told, are in progress in accordance with an agreed-upon schedule with the Office of the Comptroller General. This includes evaluations of aspects of overseas development assistance activities, such as aid decentralization. These studies could consume an increasing portion of the resources of the Division. It is important that they focus more on effectiveness measurement and less on administrative efficiency because the latter is already under the purview of internal audit. Otherwise, the Division's contribution to effectiveness measurement may again decline.

Department of National Defence - 1987, Chapter 10

Background

26.69 From 1984 to 1987 we made 48 recommendations that dealt with a broad range of the Department's systems and areas of responsibility. The Public Accounts Committee subsequently made eight additional recommendations. The Department has assisted us in our efforts to follow up on its response to these recommendations by submitting to us semi-annual reports on progress.

26.70 This report focusses on the recommendations contained in Chapter 10 of our 1987 Report, which deals with the Materiel Support system in DND, and on some of the key recommendations contained in our 1984 Report. We did not review progress related to recommendations in the areas of Human Resources Management and Major Capital Projects; these will be dealt with as part of comprehensive audits currently under way or planned.

Conclusion

26.71 The Department is taking action on most of our recommendations. In a few cases, factors external to the Department constrain its ability to move as quickly as it would like in making needed changes. Given the longer term nature of most of the departmental initiatives, it is important that interim measures be taken, so that problems do not persist until the major initiatives are completed. The Department has taken a number of initiatives of this type, and although resource limits constrain the pace at which the initiatives can be pursued, it is important that these efforts be maintained and enhanced.

Observations

Force Structure Planning and Feedback Mechanisms

26.72 In our 1984 Report we noted that DND was still adapting to the effects of the decisions to unify the forces and integrate the civilian and military components of the Department. We stressed the need for a peacetime force structure for the longer term with an appropriate link to wartime requirements, which could be used as a basis for shorter-term decisions. We also suggested improved and co-ordinated feedback on defence capabilities.

26.73 Major initiatives that have been taken include: the creation of two new organizational entities, the Chief Operational Planning and Force Development and the Chief Review Services; the production of a Canadian Forces Development Plan (CFDP), presently approved as provisional; and the development of the Operational Readiness and Effectiveness System (ORES). The impact of each of these initiatives will be realized over the long term.

Materiel Support

26.74 The 1987 audit of Materiel Support addressed six major areas: the materiel support framework; acquisition; distribution network operations; inventory management; supply support to maintenance; and management information and feedback.

26.75 We concluded that neither the materiel support system nor the logistics framework was suitably developed for sustained conflict and that, for many of the same reasons, the supply system exhibited significant economy and efficiency difficulties in peacetime. The Public Accounts Committee devoted two sessions to this Chapter.

26.76 One of the Department's most important undertakings regarding materiel support is the Canadian Forces Supply System Upgrade (CFSSU) project, which is now in the project definition stage. Originally planned for completion in the late 1980s, its anticipated completion date is now 1997. Should the CFSSU be carried out as currently proposed, it will be a positive step toward meeting many of our concerns.

26.77 **Materiel support framework.** We recommended that DND clearly define the responsibility for materiel support throughout the chain of command and that the doctrine and concepts of operation be updated to reflect current requirements. The Department has commenced work on these issues as part of the major initiatives outlined above, and through other initiatives such as undertaking Combat Development Studies and the establishment of an Aerospace Doctrine Board.

26.78 **Acquisition, inventory management and distribution.** We noted weaknesses in the training of supply managers, and this area is now being addressed. We pointed out the need for greater accuracy in the data used to determine procurement quantities; work in this area has begun and needs to be expanded. We also identified increased costs resulting from the manner in which procurement was being carried out through a co-operative logistics (COLOG) arrangement with the Department of Defense in the United States. New instructions have been written and implemented by DND and DSS for purchasing through COLOG at advantageous prices to the Crown. As a result, the value of COLOG procurement has increased from $34 million in 1986-87 to approximately $80 million in 1988-89.

26.79 Some related matters noted in our 1987 Report which may require interim measures until the CFSSU is completed include: the re-evaluation of computer formulae that recommend purchase quantities; systematic review of existing maximum stock levels; and enhanced review of the requirements determination process and the resulting purchase decisions.

26.80 In response to our observations about inventory that exceeded requirements, the Department is now reviewing 4,000 line items each month.

26.81 A matter that needs to be resolved is the management of the distribution network and improvements in information for this purpose. We were informed by the Department that preliminary studies have been conducted and work must continue in this area.

26.82 **Feedback and management information systems.** We recommended that comprehensive measures of materiel support effectiveness be established to cover the full range of Headquarters and Command materiel support responsibilities. We also recommended regularly scheduled, comprehensive Canadian exercises to fully evaluate the entire materiel support system.

26.83 The Department has included materiel support tasks in its Operational Readiness and Effectiveness System (ORES), which is still in the development stage. We are unable to conclude at this time whether it will cover the full range of materiel support responsibilities or properly report the impact of supply on equipment readiness. If the Canadian Forces Development Plan (Provisional) is approved as intended, the ORES should become fully operational by 1990. The Department has not yet taken action to evaluate the entire materiel support system as part of regularly scheduled comprehensive Canadian exercises.

Canada Employment and Immigration Commission - 1987, Chapter 14

Background

26.84 Our 1987 report addressed the development, implementation and operations of the Canadian Jobs Strategy and the financial management and control in Employment and Immigration Canada (EIC).

26.85 We examined the measures taken by EIC following our 1987 recommendations and observations. Our follow-up comprised interviews with management and employees and an examination of relevant documentation. We did not, however, perform extensive testing in the regions and local offices to corroborate management assertions.

Conclusion

26.86 Satisfactory progress has been made in the area of financial information systems. However, no policy on financial analysis for new programs has been put in place. Little progress has been made in the area of information for resource allocation and operations for the Canadian Jobs Strategy and the National Employment Service.

Observations

Canadian Jobs Strategy

26.87 **Financial analysis of recommended options**. In our 1986-87 audit, we observed that EIC had not carried out any formal financial analysis of alternative approaches when developing the Canadian Jobs Strategy program, to ensure that expenditures were made with due regard to economy.

26.88 Despite the fact that no new program has been developed since our audit, we expected that EIC would have established a policy or directives calling for a financial analysis of options to be considered when developing new programs. We did not find such a policy or directive. While EIC is of the opinion that financial analysis would not be meaningful given the multitude of uncontrollable variables in socio-political decision-making, we believe that decision makers should be provided with data on the relationship of the costs and the benefits of a new initiative.

26.89 **Projects' compliance with program directives**. During our 1986-87 examination of the Canadian Jobs Strategy, more specifically the Job Development program, we noted that a major proportion of project files we examined did not include all the information necessary on continuing employment potential, local market needs or training plans. Consequently, EIC had no assurance that all proposals for Job Development were selected and approved in accordance with program objectives or that all participants were eligible.

26.90 A new manual was published and put in place in July 1988. The manual defines responsibilities and establishes procedures to be followed by all parties involved with respect to labour market needs and training plans. We did not verify compliance with these procedures but our next audit of the Canadian Jobs Strategy will cover this.

26.91 We also recommended in 1987 that formal procedures be established to define the authority for determining and monitoring the eligibility of participants when outside organizations are involved. We found that this authority has been defined.

26.92 Finally we recommended that the client information form be amended to include the signature of each participant, attesting to his or her eligibility at the time of admission to the program. The form has been amended, to require participants to attest to information provided on it.

26.93 **Participation targets**. When the Canadian Jobs Strategy was implemented, EIC incorporated in its plans participation targets for the clientele covered by employment equity measures (for example, women, native people and visible minorities). We noted then that established targets were not realistic on a short-term basis. Since then, EIC has put a system in place that specifies both long-term and operational objectives.

26.94 Operational objectives are established by regional offices but there is no uniformity in the way they are developed. Each region has its own strategy and sets its objectives according to that strategy and to the long-term objectives developed at Headquarters.

26.95 Long-term objectives are in some cases not realistic, especially for disabled people and visible minorities in the Skill Shortages and Skill Investment programs. For the same target population, some regions are far from reaching their objectives while others have already exceeded theirs.

26.96 EIC has recognized this situation and is revising its objectives, using data from the 1986 Census. New objectives should be in use for 1990-91.

Financial Management and Control

26.97 Information for resource allocation and operations. Our 1986-87 examination of financial management and control uncovered some weaknesses. Objectives for the Employment and Insurance Program and for the Human Resource Development activity and its sub-activities were too broad; they were not sufficiently precise to serve as a basis for allocating resources, measuring performance or ensuring accountability. Moreover, for the Unemployment Insurance program sub-activities, neither the expected results nor the performance indicators were linked to the portion of the program objective which was directed to facilitating growth and adjustment in the economy. The Operational Plan Framework needed improvement, particularly in relation to the performance indicators established for the National Employment Service. We also noted that analysis of the financial and operational results of the Canadian Jobs Strategy was not integrated in reports to the National Executive Committee.

26.98 Our follow-up audit revealed that, although some efforts had been made, improvements are not yet visible in the operational results. In the context of the Increased Ministerial Authority and Accountability (IMAA) agreement signed with Treasury Board in July 1988, EIC has revised the sections of its Operational Planning Framework dealing with Human Resource Development and Unemployment Insurance. Work is progressing on the sections on Corporate and Special Service, Program Management and National Employment Services. Our examination showed that objectives have not changed, and performance indicators for the Unemployment Insurance program are still not linked to growth and adjustments in the economy. In addition, the National Employment Service has not yet completed its selection of performance indicators, as noted in Chapter 24 of this report. No change has been made to the analysis presented in the reports to the National Executive Committee on the Canadian Jobs Strategy, although two new indicators linking financial and operational results have been developed in the context of IMAA.

26.99 Financial control. In 1987 we referred to a reservation in our opinion on the financial statements of the Unemployment Insurance Account concerning the validity of the amount overcharged to the government share of expenditures on claims in 1985. Corrective measures have been taken, and we no longer have a reservation.

26.100 Financial information systems. During our 1987 examination we noted that the Employment and Immigration Information System (EIIS) did not meet some managers' requirements for timeliness, particularly those in district and local offices.

26.101 Since then, EIC has put in place a new decentralized accounting system in its 400 larger Canada Employment Centres (CEC). According to some CEC managers, this system meets most of their financial information needs on a timely basis and has eliminated most of the manual records which used to be kept in the local offices. However, there are still elements of the system to be implemented. Although the system must still be installed in 100 Canada Immigration Centres, we believe the progress made to date has been satisfactory.

Special Audits - 1987, Chapter 15

Risk Management

26.102 Our 1987 work focussed on three major capital projects where we found deficiencies in procedures for reducing the risk of losses to the Crown. For follow-up purposes we reviewed the action taken to rectify the deficiencies noted and found that progress has been satisfactory.

Microcomputer Study

Background

26.103 In 1987 this Office conducted a special study on the government's use and management of microcomputers. We also examined whether departments were realizing the benefits projected and controlling the risks inherent in acquiring and using microcomputers.

26.104 Five departments were involved in the 1987 study:

- Agriculture;
- National Revenue - Customs and Excise;
- Energy, Mines and Resources;
- Statistics Canada; and
- Transport.

Conclusion

26.105 We believe that some progress has been made since the completion of our study in 1987 and that departments are becoming more aware of the advantages to be gained from the efficient use of microcomputer technology. We are also aware that other departments, outside the scope of this study, are pressing on with innovative applications involving the use of microcomputers. However, due to the extensive amount of microcomputer evaluation, audit and policy development work now going on in different departments, it is our opinion that a further look at the situation in 1991 would be justified.

Observations

26.106 Our 1987 study observed that the microcomputer had a very significant role to play in government computer projects, but that the technology itself was not sufficiently well planned or controlled to ensure the realization of its full potential.

26.107 We found that since our study in 1987 the departments reviewed had acquired significant numbers of additional microcomputers. The number in Customs and Excise has increased from 650 to 1,300; in Statistics Canada from 750 to 1,300; and Energy, Mines and Resources (EMR) now has approximately 1,500, a ratio in that department of about one micro for every three employees.

26.108 In 1987 Treasury Board published a policy overview in the document, "Strategic Direction in Information Technology Management in the Government of Canada". This stated that adjustments to current policies were needed to take into account the merging of information technologies, human resource considerations and recent technological developments.

26.109 To this end, Treasury Board is overhauling the technology policies in the TB Administrative Policy Manual (Chapters in the 400 series). New policies on the "Management of Information Technology" are expected to be published in late 1989. Departments are contributing to these policies through a working group of the Advisory Committee on Information Management.

26.110 The computer environment in government departments is changing radically to accommodate microcomputer and communications technologies. Many new initiatives are under way incorporating these technologies, and departments are doing their best to make the most of the opportunities offered as well as fulfilling their day-to-day duties in satisfying their program and legislative responsibilities.

26.111 Major studies are under way in different departments. EMR, for instance, is studying the management of microcomputers in the Department; Statistics Canada is planning an audit of the use of microcomputer technology across the Department; Customs and Excise is moving to an integrated single technology environment; and Treasury Board is redefining all Information Technology policies to accommodate new developments and departmental requirements.

We believe our follow-up audits are useful in keeping Parliament and the Public Accounts Committee informed about actions taken by departments and agencies.

26.112 Our 1987 study recommended that departments should investigate bulk purchasing or site licences when buying microcomputer software. Some departments have examined this method of purchasing software, and in fact several have site licences for various packages, including WordPerfect and Oracle. We noted, however, that departments believe that the federal government could have more leverage, and therefore get more value for money, in microcomputer software purchases if the negotiations for bulk, site, or departmental agreements were performed by the Department of Supply and Services (DSS) on behalf of all government departments. At present each department does this independently. DSS has recently issued a series of National Master Standing Offers for the purchase of microcomputer software.

27

SPECIAL AUDITS

27

SPECIAL AUDITS

Main Points

Emergency Preparedness Canada

27.1 We found that interdepartmental co-ordination had improved since our 1987 audit. Emergency Preparedness Canada (EPC) is providing general direction to departments, but not adequate guidance about their roles or levels of response in the event of a specific emergency (paragraphs 27.18 and 27.19).

27.2 EPC is using risk analysis in its planning for earthquakes in British Columbia. EPC is considering the use of risk analysis as a complement to existing approaches in planning for national emergencies, but does not yet routinely utilize this technique (27.23 and 27.24).

27.3 Goals and deadlines for national emergency planning by departments remain inadequately specified. For example, in August 1988 EPC requested departmental planners to provide achievable dates for completion of milestones. EPC could not provide us with any specific responses to this request (27.27 to 27.29).

27.4 We found planning for National Emergency Agencies (NEA) to be inadequate. Recently passed legislation assigns various powers to the Governor in Council to enact Orders and Regulations for emergency planning and for designated national emergencies. We are concerned that there is no master plan with milestones for enactment of Orders and Regulations and that there may be gaps or overlaps with resultant confusion between the individual Orders and Regulations. Several departments have also expressed concern along these lines (27.31 and 27.32).

Courier Services

27.5 Total expenditures on courier services could not be identified accurately (27.40).

27.6 Ad hoc contracting procedures in some departments do not ensure that courier services are acquired with prudence and probity (27.42 and 27.43).

27.7 The Department of Supply and Services (DSS) obtains substantial discounts on published tariff rates for courier services. Further reductions in rates could be obtained from certain firms by consolidating locations within departments for picking up and delivering items (27.45 and 27.46).

Main Points (cont'd)

27.8 Departments have to call DSS or individual courier firms to find out the rates charged under existing agreements. If such information were readily available, departments could easily compare rates and select the least expensive firm (27.47).

27.9 Departments which negotiated directly with courier firms for specified services obtained better prices than those available under DSS Agreed Rate arrangements (27.48).

27.10 In the departments where we audited use of courier services, controls over the use of such services ranged from very good to non-existent (27.49 and 27.50).

27.11 Alternatives to courier services could be used more extensively (27.51).

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SPECIAL AUDITS

Introduction

27.12 The Special Audits group examines specific programs and activities within a department or across several departments. These topics would normally not be examined by means of comprehensive audits or government-wide audits. This approach allows the results of Special Audits to be reported quickly to Parliament and, at the same time, increases the efficiency and effectiveness of the Office.

27.13 The topics included in this year's chapter are Emergency Preparedness Canada and Courier Services.

Emergency Preparedness Canada

Background

The state of affairs two years ago

27.14 In 1987 we audited Emergency Preparedness Canada (EPC), examining in particular its legislative authority and the extent of implementation of the 1981 Emergency Planning Order for planning for national emergencies in peacetime. We found:

- a lack of statutory authority for the federal government to declare a national emergency in peacetime;
- a lack of milestones and deadlines for completing plans to achieve a state of readiness;
- the absence of a national process to identify potential risks from specific hazards, as a basis for planning national responses and identifying the resources that would be needed;
- a lack of reporting and accounting to Parliament for the state of planning for national emergencies and Canada's capabilities to respond;
- the need to re-examine and redefine the duties of the major federal responsibility centres; and
- the need to designate a federal agency responsible for co-ordinating and testing specific national emergency plans among several federal entities, and between the federal government and the provinces.

Findings

We reviewed the actions taken by EPC in response to our 1987 Report recommendations

27.15 Two new Acts -- the Emergencies Act and the Emergency Preparedness Act -- were passed by Parliament in 1988. The Emergencies Act will be proclaimed by the Governor in Council only when required to deal with one of the four types of national emergencies defined in the Act. The Emergency Preparedness Act assigns specific responsibilities to EPC for civil emergency planning.

27.16 The 1981 Emergency Planning Order was revoked when the new Acts were introduced on June 26, 1987. However, Cabinet directed all departments and agencies to continue planning for emergencies in accordance with existing government policy and the provisions of the proposed legislation. This direction lapsed with the enactment of the legislation in 1988. Orders and Regulations associated with the new legislation and required to provide for National Emergency Agencies have not yet been approved.

We found improved interdepartmental co-ordination in planning. However, we have concerns about the adequacy of guidance EPC gives to departments

27.17 We found that EPC had improved co-ordination in a number of areas, such as the work currently underway by departments in reviewing and preparing the new Orders and Regulations, establishing the Major Industrial Accidents Co-ordinating Committee, and sponsoring the Federal Working Group on National Earthquake Preparedness. The draft plan for a national response to a catastrophic earthquake is an example of a co-ordinated planning approach to national civil emergencies which cuts across departmental lines and includes provincial and local participation.

> ***We reviewed the actions that have taken place in the last two years in response to our 1987 recommendations.***

27.18 Although EPC provides general direction to departments and agencies, we have not seen evidence of adequate guidance concerning their roles or levels of response in the event of a specific emergency. Also, we have not seen evidence that EPC provides adequate guidance on how departmental resources should be allocated to emergency planning. We also found several situations where EPC did not provide sufficient information or scenarios for departments or agencies to use as a basis for detailed emergency preparedness planning. Transport Canada and Industry, Science and Technology have informed EPC about the lack of information.

27.19 Furthermore, we found that EPC was providing minimal information to emergency planners in departments with respect to shortcomings or gaps in departmental planning. EPC indicates that it is now carrying out some preliminary evaluation work.

27.20 At the end of 1988-89 EPC management approved a modified annual planning and accountability system to be implemented in 1989-90. In our opinion, this should improve the effectiveness of EPC's operations.

EPC is considering the use of risk analysis as a complement to existing approaches in planning for national emergencies but does not yet routinely utilize this technique

27.21 Our 1987 audit found there was no formal system of "national" hazard or risk assessment, that would permit co-operative federal-provincial planning and federal interdepartmental planning for potential national emergencies in peacetime, for example major oil spills. In our opinion, risk assessment would be a useful complement to the all-hazard approach to planning used by EPC.

27.22 EPC did not accept this recommendation. EPC states that its "all-hazards approach" covers the standard requirements for assistance regardless of the cause or nature of an emergency, and that risk analysis is much more appropriately done by those responsible for responding at the local or regional level.

27.23 Our current examination found that EPC is considering risk analysis and a range of probable scenarios that could be useful planning tools for responding to civil emergencies at the national level. However, EPC does not yet routinely include this technique in planning. EPC relies on the individual departments to prepare plans against scenarios of their own choosing and to communicate those with each other.

27.24 EPC is co-ordinating the preparation of a national response plan for a major earthquake in British Columbia. This is a good example of the approach we recommended. Planning for a national response is on the basis of a specific hazard to a defined area, and we note that the Geological Surveys of Canada has identified this region as a high risk area. EPC expects to complete the plan by the end of 1990.

27.25 We did not find other examples of draft plans for specific peacetime national emergencies, for example, a major toxic chemical release like the one that occurred in Bhopal, India. Further, EPC has not provided scenarios, or probabilities of risk, that departments could use as a basis for developing their response plans and resource requirements for civil emergencies, either national or regional.

27.26 EPC believes that its new program planning and accountability system will assist in addressing these concerns, since it will require an ability to maintain a current appreciation of the full range of sectoral issues, including trends in the occurrence of hazardous conditions.

Goals and deadlines for national emergency planning by departments remain inadequately specified

27.27 In our 1987 examination we found it difficult to assess progress toward the development of NEA plans because no milestones had been established. EPC agreed with our recommendation that goals and deadlines should be established for the completion and testing of plans for the NEAs.

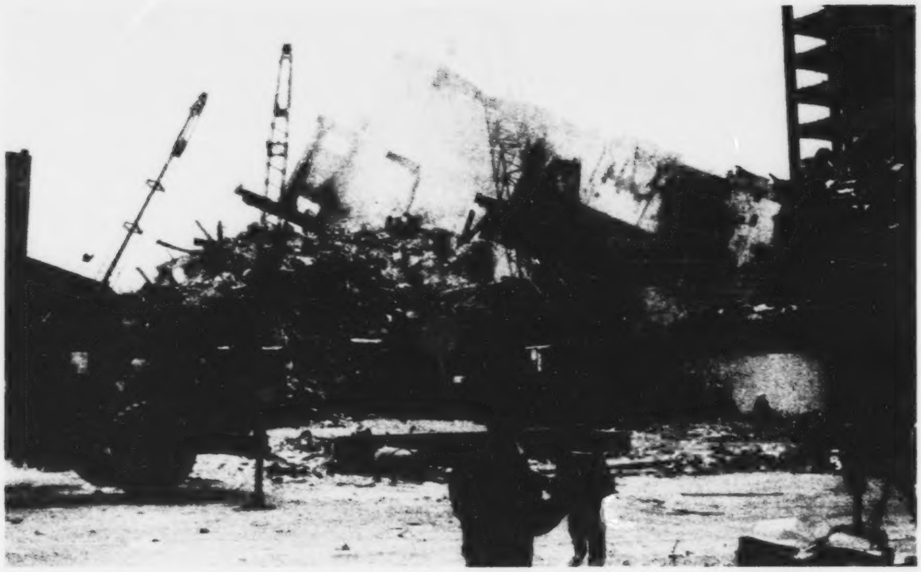
There has been progress, but much remains to be done in the area of planning for national emergencies.

27.28 In August 1988 EPC distributed a draft paper to departments on planning milestones, with an overall target for completing departmental plans. These plans are to be ready prior to the national emergency preparedness exercise (CANATEX 90) scheduled for late 1990. EPC also requested departmental planners to provide achievable dates for completion of the milestones outlined in the document. EPC could not provide us with any specific responses to this request. We found that some departments had included target dates for specific items which could be components of the milestones in information provided to EPC. However, EPC has not compiled or aggregated these into the milestones they proposed nor have they set up a master listing or schedule of milestones and targets on the basis of the NEA annual reports.

27.29 Our review of the 1988 NEA annual reports to EPC showed that five agencies reported overall target dates for completing certain projects, while four agencies did not provide this information. Only one agency -- National Emergency Construction Agency -- provided detailed information on milestones.

Information for Parliament: first report in preparation

27.30 The Emergency Preparedness Act requires the Minister responsible for EPC to report annually to Parliament on the operation of the Act during the year. At the time of our examination EPC was collecting and compiling information on the status of NEA plans for



1985 Mexico City earthquake - estimated 10,000 deaths, and 200,000 people lost homes - EPC is co-ordinating a plan to deal with the possibility of earthquakes in British Columbia.

inclusion in the first report, which will be tabled within 15 sitting days after June 30, 1989. We were informed that EPC will provide some general comments with respect to the NEA planning activities.

We found the process for designating lead agencies for planning for emergencies to be inadequate

27.31 Our 1987 audit noted a need for designating lead departments for specific national emergencies and for updating these designations and their responsibilities on a regular basis.

27.32 The new legislation assigns various powers to the Governor in Council to enact Orders and Regulations for emergency planning. The departments concerned and the Department of Justice are currently reviewing what should be provided for in such Orders and Regulations. This work is being co-ordinated through EPC. However, we are concerned that there is no master plan with milestones for enactment of Orders and Regulations and that there may be gaps or overlaps, with resulting confusion between the individual Orders and Regulations. Several departments have also expressed concern along these lines.

27.33 In the case of four exercises scheduled for 1989-90, lead agencies have been identified for planning and testing.

Courier Services

Introduction

27.34 Government departments and agencies use commercial and departmental courier services extensively and increasingly: $14.5 million was spent for courier services in 1988-89, compared to $6.9 million in 1982-83.

27.35 Courier services range from small local operators using cars and bicycles to major international corporations which own and operate their own aircraft and other major transportation facilities. They also include the use of Priority Post Services of the Canada Post Corporation.

27.36 The services used by government departments and agencies include:

- inter-city services connecting all large and most smaller urban centers in Canada, and having connections or services to the United States, Europe, Japan and other countries.
- services within cities, that pick up and deliver either on request or on a schedule.
- contracted regional or local mail and messenger service with regular pick up and delivery, with or without provision for additional services on demand.

27.37 Departments obtain courier services by:

- awarding contracts with fixed terms and prices for services.
- accepting offers from firms to provide services at the rates specified by the firm. These offers may be formal agreements or informal arrangements whereby services are requested and invoiced.
- calling up couriers who have entered into agreed rate arrangements with the Department of Supply and Services.

Audit Objectives and Scope

27.38 The objectives of this audit were:

- to identify the extent and cost of courier use by departments and agencies;
- to determine if these services are acquired and managed with due regard for economy; and
- to determine the availability and use of alternatives to courier services, such as facsimile transmissions, electronic mail, etc.

Government departments use courier services extensively and increasingly. In 1982-83 the cost was $6.9 million; by 1988-89 it had climbed to $14.5 million.

27.39 We reviewed the Department of Supply and Services' (DSS) procedures to obtain negotiated government-wide rates for courier services. We also examined procedures for the acquisition and management control of courier services in the departments of Fisheries and Oceans, Justice, External Affairs, and Energy, Mines and Resources. We did not review DSS' use of courier services for its own operational purposes. We interviewed four courier firms that provide services in the National Capital Region, and Canada Post officials responsible for Priority Post Services. The operation of the diplomatic courier service in the Department of External Affairs was not examined.

Observations

Total expenditures on courier services could not be identified accurately

27.40 The Receiver General's Financial Reporting Statements are based on data provided by departments. The statements include a category for expenditures for courier services. However, the term "courier services" is not defined. As a result, departmental reporting practices may not be consistent or complete. For example, the departments we audited identified expenditures for Priority Post as postage rather than as courier services. One department believed it was appropriate to include travel expenses of departmental staff engaged in courier services.

27.41 The lack of reliable reporting makes it difficult to identify expenditures and make comparisons.

Ad hoc contracting procedures in some departments do not ensure that courier services are acquired with prudence and probity

27.42 Treasury Board Officials informed us that the acquisition of courier services is covered generally in existing contract directives. In two of the four departments we examined, procedures for selecting couriers were clearly set out for specific services. In the other two departments there were no procedures stipulated for acquiring courier services. In one department, the person acquiring courier services had not been formally delegated the authority to do so.

27.43 As a result of these differences in the departments we audited, the adequacy of acquisition and management practices varied. We found instances where courier companies were utilized without competitive contracting procedures. In some instances there was no contract and the decision as to which courier(s) to use was left to the shipper or mail room personnel.

Departments that negotiated directly with courier firms for specified services obtained better prices

27.44 The Department of Supply and Services enters into agreed rate arrangements at the request of any courier firm that meets DSS requirements with respect to licensing and financial solvency. It assesses the proposals submitted by each firm for the reasonableness of its proposal relative to the type of service and volume of business likely to be available. DSS' mandate to negotiate such agreements is derived from its role as a common services agency.

27.45 We found that DSS receives a substantial discount on published tariff rates. Depending on such factors as volume and competition, various types of discounts, including ones similar to or better than those obtained by DSS, are available to businesses.

27.46 Our discussions with certain courier firms indicated that rates could be further reduced if departments were to consolidate locations for picking up and delivering items.

27.47 We also found that departments have to call DSS or individual courier firms to find out the rates charged by firms under existing agreements. If such information were readily available, departments could easily compare rates and select the least expensive firm.

27.48 We found that departments which negotiated directly with courier firms for specific services obtained better prices than those available under DSS agreed rate arrangements.

We recommended that departments ensure that their use of courier services is cost-effective.

DSS calls for tenders or competitive bids when a department requests it to tender for a specified courier service.

In the departments where we audited use of courier services, controls over use of such services ranged from very good to non-existent

27.49 We found that the Department of Fisheries and Oceans in Ottawa had satisfactory procedures for contracting and monitoring the use of courier services. The Department has developed and implemented a low-cost computerized system for their Ottawa registry operations, including mail and special services. The Department also had an active program to employ disabled persons in courier service activity.

27.50 In contrast, in one of the departments we audited, individuals could use their own discretion as to whether to call a courier service or use departmental personnel to deliver envelopes or packages. The use of departmental staff for this purpose was not monitored.

Alternatives to courier services could be used more extensively

27.51 Facilities such as facsimile transmission equipment and electronic mail are used extensively in the departments we examined, particularly for inter-city and international purposes. However, they are not as extensively used locally, such as in the National Capital Region (NCR) where long-distance charges are not involved. One department estimated that increasing the use of such equipment in the NCR would reduce its requirement for local courier services by up to 50 percent, for an annual cost saving of about $18,000. Another department estimated its savings would be in the order of 20 percent, but the department's information on costs was not reliable enough to translate that saving into dollars.

Recommendations

27.52 DSS should make readily available to departments comparative information on courier rates charged by different firms.

27.53 Departments should encourage and promote the use of less expensive alternatives to courier services wherever feasible and economic.

Our audit identified a variety of means by which courier services could be provided more economically. As well, alternatives such as facsimile transmission could be used more extensively.

27.54 Departments should develop clear directives for using courier services and should consolidate pick-up and delivery locations.

27.55 Rather than relying solely on DSS agreed rate arrangements, departments should assess the cost-effectiveness of using a competitive process to acquire courier services, particularly where they can specify the nature of the service required.

27.56 Where cost-effective, departments should develop low-cost systems to monitor the use of courier and related services.

27.57 The Office of the Comptroller General should define the term "courier services" for financial reporting purposes.

Departmental Responses

Office of the Comptroller General

The Office of the Comptroller General has informed us that "a definition of courier services for financial reporting purposes has been included in the revision of the List of Descriptions for Economic, Source and Class Objects issued in July 1989".

Department of Supply and Services

With respect to the availability of information on courier rates, DSS states:

Departments are made aware of these rates through Traffic Management Bulletins and seminars on an irregular basis, as well as through the results of Central Freight Services audits. Clients can also receive comparative rate information by telephone from the Transportation Advisory service. DSS intends to increase the frequency of Traffic Management Bulletins, including rate notices, and is examining other means by which comparative information on rates could be more widely disseminated.

With respect to the obtaining of better prices through tendering:

The department has had underway, since June of 1988, a comprehensive review of its role as a service agency, under the general title of service line studies. The acquisition service line forms a major part of those studies which are in process, and specifically scheduled for review as a service line in its own right is the area of traffic management, including courier service. In essence, through this study, which will involve other government departments and central agencies, we will address the issue of method of supply most appropriate to the interests of government as a whole for the acquisition of traffic management services.

28

ORGANIZATION AND PROGRAMS OF THE OFFICE OF THE AUDITOR GENERAL

28

ORGANIZATION AND PROGRAMS OF THE OFFICE OF THE AUDITOR GENERAL

Main Points

28.1 This chapter describes the organization and activities of the Office and highlights some of our major initiatives undertaken or completed during the past year. It also describes the role of the Auditor General, the requirements of the Auditor General Act and the three types of audits the Office performs: attest, authorities and value-for-money (paragraphs 28.10 to 28.33; 28.109 to 28.119).

28.2 The Office has proposed amendments to Sections 4, 8 and 11 of the Auditor General Act (28.34 to 28.40).

28.3 Methodology development has moved ahead, with the publication of two audit guides (Auditing Financial Management and Control, and Auditing Capital Asset Projects), and research into the scoping of value-for-money audits. The scope and objectives of the Comprehensive Auditing Manual revision project have been expanded to include a comprehensive review of audit-related policies (28.41 to 28.43).

28.4 The Office has continued to upgrade its use of technology in auditing and internal communications, currently focussing on tools for analysis, creation, communication and management (28.44 to 28.63).

28.5 The Office has used alternative means of communicating audit results: videos of four annual report chapters; a booklet presenting main points of all annual report chapters; and an electronic version of the annual report with a text-retrieval software package (28.66 to 28.70).

28.6 Two outside organizations have presented awards to the Office (28.71 to 28.75).

28.7 The Program Evaluation and Internal Audit Group has assessed the work, practices and procedures of the Office through various surveys and reviews (28.79 to 28.91).

28.8 The Office participated in four major international projects this year: an international fellowship program; a review of the NATO audit system; the Sino-Canadian Auditor Training Project; and the INTOSAI (International Organization of Supreme Audit Institutions) Development Initiative, which designs and conducts training projects for groups of countries throughout the world (28.92 to 28.108).

28.9 Progress and innovations have been realized in the areas of curriculum implementation, employment equity and stress management training (28.64 to 28.65, 28.76 to 28.77, and 28.78).

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ORGANIZATION AND PROGRAMS OF THE OFFICE OF THE AUDITOR GENERAL

28.10 The Auditor General Act stipulates that "the Auditor General shall report annually to the House of Commons on the work of his Office..." The preceding chapters of this annual report describe the results of Office audit projects completed, with reports prepared for publication, during the last 12 months.

28.11 This chapter reports on other work carried out in the Office of the Auditor General (OAG), such as methodology development and major international projects. It also describes the role and mandate of the Auditor General, including the types of auditing and reporting involved; the organization of the Office; and its use of financial resources. It describes proposed amendments to the Auditor General Act. And it reports on the Office's initiatives in information technology, staff training, communication, and employment equity, as well as on the internal evaluation of its work, practices and procedures.

Mandate, Auditing and Reporting

Principles Underlying the Role of the Auditor General

28.12 The role of the Auditor General rests on three principles. The first is that the government of the day has an obligation to account to the people of Canada for its use of public funds. It must ensure that funds are raised properly, protected from loss and spent only for the purposes approved by Parliament, and that value is obtained for money spent.

28.13 The second principle is that members of Parliament have the responsibility to scrutinize the affairs of government. To assist in that scrutiny, the government must supply parliamentarians with complete and understandable information on how it has carried out its activities.

28.14 The third principle is that there must be a knowledgeable and impartial person with a mandate to examine the information supplied to MPs by the government to make independent examinations of government departments, agencies and programs and to report significant matters to MPs, so that they can fulfil their responsibility -- rooted in history, tradition and law -- of holding the government accountable for its actions.

28.15 In our system, this independent person is the Auditor General. The information he provides to Parliament is contained primarily in his annual report. It has been said that MPs are elected to the House of Commons to serve their fellow Canadians. The Auditor General is, then, the servant of the servants of the people.

The Auditor General Act and its Requirements

28.16 The activities of the Office of the Auditor General are governed by the Auditor General Act of 1977. In essence, the Act requires the Auditor General to fulfil what may be termed a traditional financial auditing role as the auditor of the accounts of Canada. As well, it requires him to call attention to anything that he considers to be of significance and of a nature that should be brought to the attention of the House of Commons. Among other matters, the Auditor General must report "any cases in which he has observed that...money has been expended without due regard to economy and efficiency; or satisfactory procedures have not been established to measure and report the effectiveness of programs, where such procedures could appropriately and reasonably be implemented".

28.17 This chapter is not the place to spell out in detail how the Office goes about its work. However, it may be useful to say something about the activities behind this annual report.

Three Types of Auditing: Attest, Authorities, and Value-for-money

Attest auditing

28.18 To fulfil his mandate as Parliament's auditor, the Auditor General is required to examine the Public Accounts of Canada and to express an opinion as to whether they present information fairly, in accordance with the stated accounting policies of the federal government and on a basis consistent with that of the preceding year, and express any reservations that he may have.

28.19 Traditional "attest" auditing of all government departments and agencies is done each year, culminating in the "Opinion and Observations by the Auditor General on the Financial Statements of the Government of Canada", which constitute Chapter 2 of the annual report.

28.20 In addition, the Auditor General expresses a separate audit opinion on the financial statements of each Crown-owned corporation and agency for which he is named auditor.

Authorities auditing

> ***The Auditor General must report annually on the work of his Office. The preceding chapters summarize audit work completed in 1989. This chapter describes additional projects, special initiatives and particular aspects of the way the Office works.***

28.21 There is a further aspect to this annual component of the Office's work. It is essential that a parliamentary auditor be able to provide assurance to members of Parliament that legislative authorities have been complied with and that public money has been spent for the purposes voted by Parliament. This extends the attest function to encompass what the Office refers to as "authorities auditing". OAG auditors identify occasions where, for example, payments have been made in advance of need, authorities have not been complied with, and similar matters. Where the Auditor General has deemed these to be significant and of a nature that should be brought to the attention of the House of Commons, they are included in the annual report.

Value-for-money auditing

28.22 The scope of the Office's auditing then widens to encompass a broader examination of selected departments, agencies and programs. For departments, this examination is performed on a cyclical basis, covering an entire department or specific programs within a department. It represents a logical extension of the attest and authorities audit, to determine whether expenditures have been made with due regard to economy and efficiency or satisfactory procedures have been established to measure and report the effectiveness of programs.

28.23 Value-for-money auditing has been steadily evolving in recent years, and its importance is recognized internationally by governments and by the accounting community. Canada is an acknowledged world leader in this field.

28.24 The value-for-money auditor establishes reasonable criteria for the efficient and economic operation of a particular entity and evaluates the organization's actual performance against those criteria. This kind of auditing requires specialized skills and, in addition to accountants, the Office employs engineers, economists, statisticians, lawyers, mathematicians, computer scientists and actuaries, together with specialists in management and effectiveness evaluation.

28.25 When an audit of a department encompasses all three components -- attest, authorities and value-for-money -- the OAG refers to it as a comprehensive audit (see Exhibit 28.1).

28.26 The Office also applies comprehensive auditing methods in its examinations of government-wide activities, or activities conducted in several departments. This year such examinations are reported in the chapters on Incentive Awards and Major Capital Projects and in the Special Audits chapter on Courier Services and Emergency Preparedness Canada.

28.27 Amendments to the Financial Administration Act in 1984 extended many of the elements of comprehensive auditing to the special examinations of Crown corporations. The Auditor General of Canada is solely or jointly the designated auditor and special examiner for many of these corporations. More information on this activity is included at the close of this chapter. Also Chapter 5 of this report gives a full account of the implementation of the 1984 framework for control and accountability of Crown corporations.

Organization

28.28 Exhibit 28.2 is an overview of the organizational structure of the Office, showing the functions of its three branches.

A description of the organization and activities of the Office's three branches

29.29 Audit Operations is the largest branch, with Department and Agency Audit Groups, a Crown Corporations Group, two Regional Audit Groups and a Planning and Co-ordination Unit. Each of the audit groups for departments and agencies is headed by an Assistant Auditor General and each is responsible for a mix of entities that require similar audit skills and special expertise or that have strong program interrelationships. The largest concentration of auditors works in the National Capital Region, but work is also carried out in the Eastern Region, with offices in Halifax and Montreal, and in the Western Region (Vancouver, Edmonton, Regina and Winnipeg). Both the Eastern and Western regions are headed by Assistant Auditors General. There are also staff from the Western Region working more or less continuously in Yellowknife, where the Office now has its own facilities, and in Whitehorse. The Planning and Co-ordination Unit, headed by a senior Principal, is responsible for strategic, operational and human resource planning and for overall co-ordination of the Branch's work

28.30 Professional Services provides professional and technical support to Audit Operations. The Branch reviews, edits and publishes the annual report and other reports. It is also responsible for professional development, methodology development, liaison with Parliament, public affairs, communications, the Office library, and legal services. Although the Branch has provided legal services for many years, during the past year a legal section was established under a newly-appointed Principal, who has functional responsibility for providing legal services and, when necessary, engaging outside legal counsel. The section provides legal advice and opinions to the Auditor General, the Executive Committee, the

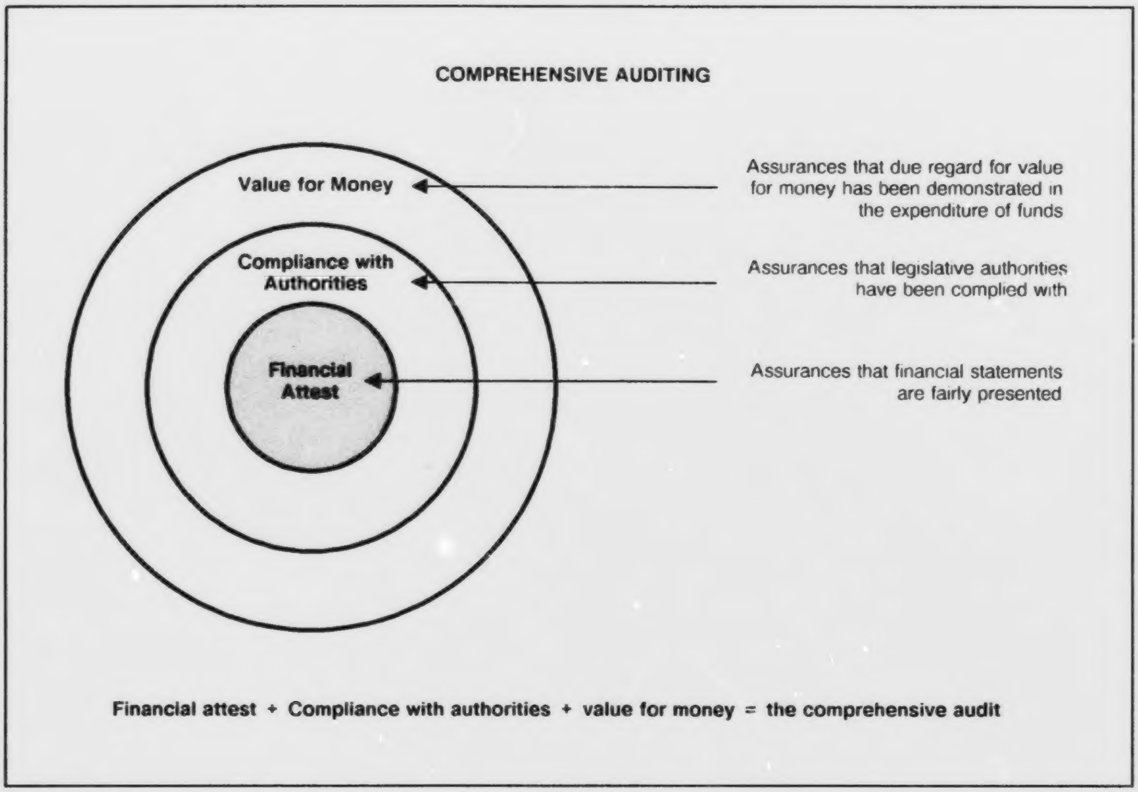

COMPREHENSIVE AUDITING
Value for Money
Compliance with Authorities
Financial Attest
Assurances that due regard for value for money has been demonstrated in the expenditure of funds
Assurances that legislative authorities have been complied with
Assurances that financial statements are fairly presented
Financial attest + Compliance with authorities + value for money = the comprehensive audit

Exhibit 28.1

Deputy Auditors General, and the Audit Operations Branch, and provides general legal support to Office activities.

28.31 The Administrative Services Branch provides central support in finance, personnel, contracting, official languages, records, facilities, materiel, EDP services, word-processing, graphics and audio-visual services.

Financial Resources

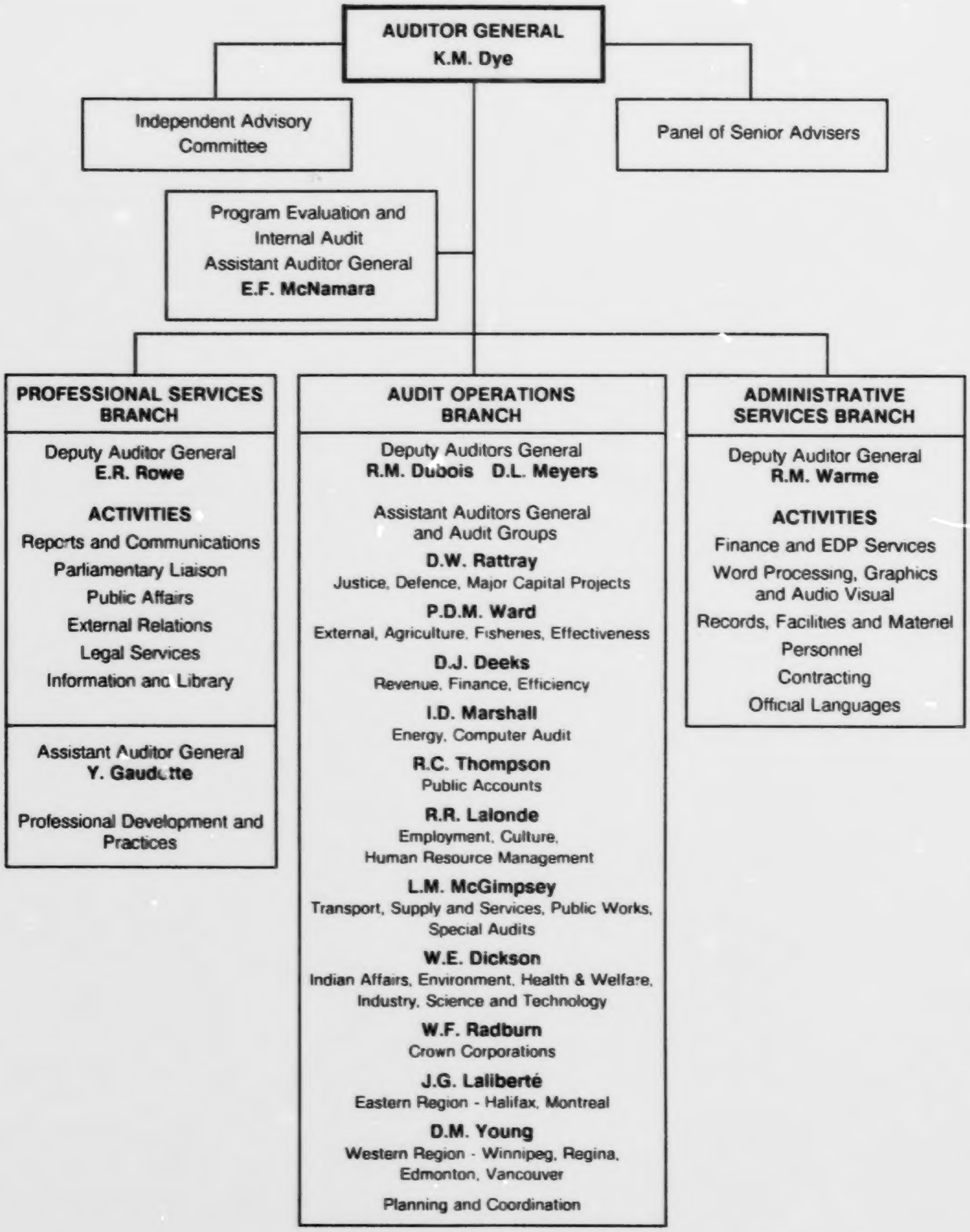
28.32 Parliamentarians now have available, in Part III of the Estimates of the Government of Canada, the detailed resource requirements of the Office of the Auditor General.

28.33 Exhibit 28.3 provides an overview of appropriations and expenditures by activity.

Proposed Amendments to the Auditor General Act

28.34 The Office has proposed amendments to Sections 4, 8 and 11 of the Auditor General Act.

ORGANIZATION OF THE OFFICE OF THE AUDITOR GENERAL
August 1989


AUDITOR GENERAL
K.M. Dye
Independent Advisory Committee
Panel of Senior Advisers
Program Evaluation and Internal Audit
Assistant Auditor General
E.F. McNamara
PROFESSIONAL SERVICES BRANCH
Deputy Auditor General
E.R. Rowe
ACTIVITIES
Reports and Communications
Parliamentary Liaison
Public Affairs
External Relations
Legal Services
Information and Library
Assistant Auditor General
Y. Gaudette
Professional Development and Practices
AUDIT OPERATIONS BRANCH
Deputy Auditors General
R.M. Dubois D.L. Meyers
Assistant Auditors General and Audit Groups
D.W. Rattray
Justice, Defence, Major Capital Projects
P.D.M. Ward
External, Agriculture, Fisheries, Effectiveness
D.J. Deeks
Revenue, Finance, Efficiency
I.D. Marshall
Energy, Computer Audit
R.C. Thompson
Public Accounts
R.R. Lalonde
Employment, Culture, Human Resource Management
L.M. McGimpsey
Transport, Supply and Services, Public Works, Special Audits
W.E. Dickson
Indian Affairs, Environment, Health & Welfare, Industry, Science and Technology
W.F. Radburn
Crown Corporations
J.G. Laliberté
Eastern Region - Halifax, Montreal
D.M. Young
Western Region - Winnipeg, Regina, Edmonton, Vancouver
Planning and Coordination
ADMINISTRATIVE SERVICES BRANCH
Deputy Auditor General
R.M. Warme
ACTIVITIES
Finance and EDP Services
Word Processing, Graphics and Audio Visual
Records, Facilities and Materiel
Personnel
Contracting
Official Languages

The Executive Committee is composed of the Auditor General and the Deputy Auditors General.

Exhibit 28.2

A legal services section was established in 1989. Directed by a Principal (centre), the section provides legal advice and opinions (see paragraph 28.30).

Amendment to Section 4: with respect to salary, pension and allowances for the Auditor General

28.35 At present, the Auditor General may choose a pension plan under the provisions of either the Public Service Superannuation Act, or the Diplomatic Service (Special) Superannuation Act. Under the provisions of both these Acts, pension payment is deferred until at least 60 years of age, and the benefits payable are based upon length of service. The Auditor General's term of office is limited to a statutory period of 10 years. Therefore, if appointed from the private sector, the Auditor General cannot accumulate sufficient service to provide a reasonable pension on retirement from the Office.

28.36 In many respects the appointment of an auditor general is analogous to the appointment of a judge. The Auditor General is paid a salary equal to a judge of the Supreme Court. Both judges and the Auditor General have statutory limitations placed upon the length of employment. The Judges Act contains provisions to provide relief from a reduced pension caused by a statutory limit on length of service. As the situation of the Auditor General is similar in this respect to that of a judge, the Office proposes that the provisions of the Judges Act, with necessary amendment, apply. It is desirable that adequate pension provisions be available to recruit the appropriate candidate. The matter is being seriously considered by the government.

Amendment to Section 8: to allow for completion date reporting rather than annual reporting by the Auditor General

28.37 The impetus for the requested amendment comes not only from the Office but also from the Standing Committee on Public Accounts. Two comparable audit entities, the National Audit Office of the United Kingdom and the General Accounting Office of the United States, have legislation allowing for completion date reporting. The proposed amendment would be in addition to the reporting required under subsection 7(3) of the Act, meaning the Office would continue to publish an annual report containing a summary of the work of the preceding year.

OFFICE OF THE AUDITOR GENERAL OF CANADA
APPROPRIATIONS AND EXPENDITURES

Appropriations and Expenditures by Activity

(thousands of dollars)

	1989-90	1988-89		1987-88	
	Estimates	Appropriations	Expenditures	Appropriations	Expenditures
Legislative Auditing	$ 50,923	$ 48,505	$ 48,441	$ 47,046	$ 45,644
TOTAL	$ 50,923	$ 48,505	$ 48,441	$ 47,046	$ 45,644

Appropriations and Expenditures by Object

(thousands of dollars)

	1989-90	1988-89		1987-88	
	Estimates	Appropriations	Expenditures	Appropriations	Expenditures
Salaries and Wages	$ 31,895	$ 29,660	$ 28,753	$ 29,931	$ 26,811
Contributions to Employee Benefit Plans	4,848	4,665	4,665	4,748	4,748
Transportation and Communications	2,850	2,920	3,206	2,918	2,969
Information	225	238	286	273	248
Professional and Special Services	6,500	7,050	7,045	6,659	6,052
Rentals	270	300	268	262	359
Purchased Repair and Upkeep	510	396	517	296	279
Utilities, Materials and Supplies	832	661	723	350	1,010
Capital-Construction or Acquisition of Machinery and Equipment	2,498	2,133	2,493	1,149	2,708
Transfer Payments	488	472	471	450	449
All Other Expenditures	7	10	14	10	11
TOTAL	$ 50,923	$ 48,505	$ 48,441	$ 47,046	$ 45,644

Exhibit 28.3

28.38 More frequent reporting would permit greater efficiency in the use of Office resources. It would allow the Auditor General to serve the House of Commons in a more timely manner. Parliament would have a better opportunity to deal with problems when they arise. More timely and effective remedial action would then be possible. Completion date reporting would also make the workload of the PAC more manageable. The PAC could deal with individual audit reports, allowing it to focus more attention on individual issues.

Amendment to Section 11: to allow the Governor in Council greater latitude with respect to the types of requests he may make of the Auditor General

28.39 Under Section 11, the Auditor General may inquire into and report on matters relating to the financial affairs of Canada, public property or any person or organization that has received or is seeking financial aid from the government of Canada if the Governor in Council so requests. On occasion, the Auditor General has been requested to provide assistance which does not fall strictly within the bounds of his authority. For example, the Office has provided assistance to the Canadian International Development Agency, the North Atlantic Treaty Organization and the United Nations. There is some uncertainty that this type of assistance could have been the subject of a Governor in Council request as the section now reads.

28.40 The Office proposes that the wording of Section 11 be changed to provide that the Governor in Council may request the Auditor General "to inquire into and report upon or assist" any of the organizations or persons covered by this provision. This change would give the Governor in Council greater scope in making requests and it would ensure that the Auditor General had the authority to perform the tasks requested.

Methodology Development

28.41 During 1988-89 the Methodology Development Committee (MDC), chaired by the Auditor General, moved energetically to implement the strategic plan developed last year. By September 1988 it had agreed upon revised operating procedures and the Committee was strengthened by adding two senior professionals.

28.42 Although methodology development and research are, by their nature, long-term activities, results are already evident from the work done during 1988-89:

- The MDC expanded the scope and objectives of the Comprehensive Auditing Manual revision project to include a comprehensive review of audit-related policies. Deputy Auditors General Edward Rowe and Raymond Dubois are directing this review. The Methodology Development Committee expects to approve all policies by the fall of 1989.

- The MDC has approved publication of audit guides reflecting up-to-date experience in auditing particular facets of government operation. The Committee has approved publication of two guides: Auditing Financial Management and Control and Auditing Capital Asset Projects. The MDC has also approved a position on how the Office will implement the value-for-money auditing standards proposed by the Canadian Institute of Chartered Accountants (CICA).

- The MDC has launched research, under the guidance of Deputy Auditor General Larry Meyers, into the scoping of value-for-money audits. This applied research project is designed to help senior management provide clearer direction for audit staff.

The official launching of a new audit guide entitled Auditing Capital Asset Projects. The aim of the new guide is to help the Office's professional staff understand the process involved in auditing capital asset projects (see paragraph 28.42).

28.43 During the past year, the Office has modified its approach to development projects to more effectively balance cost, time and quality. Among the changes that have been made are greater use of task forces rather than standing committees and more recognition of staff who participate in methodology development projects. Finally, there has been greater involvement of government managers, through participation on task forces and circulation of formal exposure drafts, to ensure that Office criteria and approaches provide a mutually agreed-upon basis for audit.

Information Technology

The Evolution of Information Technology in the Office

28.44 Although the Office had acquired one microcomputer in 1979 and a variety of word processors in the late 1970s and early 1980s, the adoption of general purpose personal microcomputer technology did not begin until 1983. Since then, the Office has continued to expand the use of electronic technology, acquiring additional units and extending interconnection to improve the productivity and quality of audit work.

28.45 At first, the Office acquired commercially available software for applications that business and industry as a whole found valuable: word processing, spreadsheets, data bases and communication. As early as 1984, the Office began to analyze its needs with more precision and subsequent software acquisition and development was tailored to the specific needs of auditors. Since 1985, one group in the Office has piloted new hardware and software innovations before their release for use by the rest of the Office. Now many of these products are widely used by other groups and teams

28.46 Currently, the Office's principal focus in information technology is on tools for analysis, creation, communication and management.

Tools for Analyzing Data, Systems and Text

28.47 Auditors are concerned with the analysis of both structured data and continuous text. In addition, auditors frequently need to document complex systems graphically.

28.48 IDEA (Interactive Data Extraction and Analysis) helps auditors use microcomputers as powerful analytical tools. It is now used not only by this Office but by public and private audit organizations throughout the world. The move to laptop computers has enabled auditors to apply this, and other tools and technology, directly at client locations.

28.49 I Chart is a flowcharting program to facilitate the documentation of complex systems and processes that must be audited. This program is now used extensively by audit teams throughout the Office.

28.50 Text retrieval-Ful/Text: Text-retrieval techniques have been brought to the auditor's laptop computer to permit the quick and efficient searching of large quantities of text such as statutes, regulations and reports. Electronic versions of the Auditor General's annual reports from 1983 to 1988 are available, as are most audit guides, the Office's Comprehensive Auditing Manual and a variety of statutes and regulations. They are operated with a user-friendly text-retrieval software package called Ful/Text.

28.51 Experimental work has begun on a compact disk (CD-ROM) that would contain all relevant material needed by field auditors and researchers.

Tools for Creating

28.52 Auditors often create spreadsheets to document the results of their work, but their principal output is usually a written report. The Office provides every auditor with access to powerful application programs for both. For authors, a program for checking grammar and style is available.

28.53 ReportRead: Annual report chapter authors, together with the Auditor General and Deputy and Assistant Auditors General and other chapter reviewers, can access the report electronically on a microcomputer as it develops. ReportRead has eliminated much of the need to photocopy and distribute hard copies of the chapters. ReportRead greatly facilitated the review of the 1988 Report, and an improved version has helped even more this year.

Tools for Communicating

28.54 Tools for internal communications: electronic mail - One of the Office's routine means of communicating, in headquarters, between audit sites in Canada, and throughout the world, is electronic mail. The Office now has close to 500 users. Electronic bulletin boards are used to exchange documents, information, comments and review.

28.55 Tools for external communications: electronic publishing - The Office experimented this year with distribution of an electronic version of the 1988 Report, with full text-retrieval capability. Copies were supplied to government departments, libraries and corporations, both in Canada and in other countries, and were installed on request in offices of several members of Parliament.

Search with Fultext
Recherche a l'aide de Fultext

The Auditor General unveiled a new OAG product that has proven to be a valuable research tool. It is an electronic version of the annual report together with a user-friendly text-retrieval software package for easy access to any of its information (see pararaph 28.50).

Tools for Managing

28.56 Managing an audit: the electronic briefcase - The Office is now implementing, in phases, the micro-based system AuditPro, which enables auditors to use the computer to better plan and control audit tasks and working papers. Many types of software can be linked to AuditPro. Eleven audit teams are now using the system; in field use it is proving that it can save hundreds of audit hours and should result in significant quality and effectiveness improvements over the next few years. AuditPro also provides senior auditors with an easy and structured method of reviewing electronic working papers.

Managing the Office using a new computerized management information system: MIS 2000

28.57 The Office of the Auditor General began developing a new management information system, MIS 2000, in the fall of 1988, to replace the present system which has been in use since 1982. An on-line integrated financial and operational management information system, it is expected to meet all the Office's needs until at least the turn of the century.

28.58 In the fall of 1988, the Administrative Services Branch conducted an Office-wide user needs analysis which identified the specifications and features required to tailor the new computer to Office-wide applications.

28.59 A key feature of MIS 2000 will be that the Office can use its network to create and access automated services. For example, it will provide an improved in-house electronic mail network; it will allow sharing of printing facilities; and it will create electronic filing systems.

28.60 As well as providing on-line management information for its principal users in Audit Operations, MIS 2000 will also handle the Office's financial statements and the requirements of support groups such as contract administration, professional development, materiel management and personnel. In short, it will be able to accommodate almost any identified user need.

MIS 2000 will be a fully integrated financial and operational management system providing on-line information to its principal user, Audit Operations. It will also handle the financial statements and requirements of the other branches of the Office (see paragraphs 28.57 to 28.61).

28.61 The objective of MIS 2000 is to have an overall integration of all data bases which will contribute to a more effective and efficient audit office. The MIS 2000 project is scheduled for complete implementation in 1991.

Training Office Staff in the Use of Information Technology

28.62 Innovation in information technology is not possible without a corresponding investment in staff training. Under the Auditor Trainee program begun in 1985-86, about 10 auditors per year spend approximately 12 months with the Computer Audit Group, acquiring practical experience in EDP auditing practices. Most groups in the Office now have a trained EDP auditor.

28.63 A more recent initiative is the Administrative Staff Microcomputer Apprenticeship Program. The program provides selected audit support staff with four months of intensive upgrading of skills, using computer tools and techniques like word processing, text retrieval, spreadsheet preparation, flowcharting and electronic mail programs, before they return to their regular audit team duties. There they are able to provide support and guidance to auditors using these tools.

Core Training Curriculum Implementation

28.64 The Professional Development and Practices Group completed a survey in 1988 on the anticipated training needs of auditors for the next three years. This survey was based on a Core Curriculum for Auditors, developed the previous year, which represents the key knowledge and skills required by audit staff to perform their work.

28.65 A training plan was drawn up based on the survey and implementation began this year. The plan includes updating some courses, developing new ones, and incorporating recently developed audit software into these courses.

Alternative Means of Communicating Audit Results

28.66 In addition to the annual report, the Office uses other means to communicate the results of its audits and make them more accessible to interested parties. In 1988, the third year of a pilot project, the Office produced videotape summaries of three audit report chapters and a fourth, outlining the Auditor General's Opinion on the Financial Statements of Canada. The three chapters selected were Well-Performing Organizations; Energy Mines and Resources - the Management of Federal-Provincial Contribution Programs; and Fisheries and Oceans - Atlantic Operations, Inspection and Corporate Functions. The videos were made available to MPs at a preview briefing, and to the media at the press "lock-up", on annual report tabling day. They were viewed continuously throughout the morning and segments were used that evening in national, regional and local news broadcasts. Immediately after the report was tabled by the Speaker, the videos were placed on the House of Commons internal cable system (OASIS) for viewing on demand by members of Parliament. The OAG received over 75 requests for complete sets of the videos as well as requests for individual video chapters. Requests came from individuals as well as from federal government departments, audit organizations, colleges and universities, television stations and cablevision outlets.

28.67 An innovation in 1988 was the production of a pocket- or purse-size booklet, which presented the main points from each of the chapters in the annual report. Paragraph references at the end of each main point provided quick access to more detailed information in the report. Reaction from the media and the public suggested that this was a needed report-in-brief that the ordinary taxpayer could find time to read.

28.68 A second innovation, previously mentioned in the section on information technology, was unveiled by the Auditor General on tabling day -- an electronic version of the annual report, with a user-friendly text-retrieval software package for quick access to desired information. It could prove to be a valuable research tool for members of Parliament and their staffs. To use the package, the software is loaded into appropriate equipment and screen prompts are followed to search the text using key words or phrases. The section of text related to the chosen topic can be displayed, or the user can "browse" through sections that appear to be interesting. The package can be mastered in a few minutes by anyone with a basic familiarity with computers.

28.69 The research use for this electronic report will be to gain fast, accurate and easy access to comments made by the Auditor General on particular departments, agencies and their related programs. The text can also be searched for comments on broader issues like efficiency, the environment or human resource management. This search capability offers obvious research applications for members of Parliament in a number of areas, including preparing for Question Period, responding to constituent queries and preparing to take part in debates.

28.70 In addition to the current year's report, the Office has converted annual reports back to 1983 to this electronic format. Primarily because of its size, this is not being distributed; however, it can be accessed through the OAG Library or the OAG Parliamentary Liaison Group. It can be used to identify quickly whether and when in the past six years the Auditor General has commented on a particular topic of interest.

Two Awards From Outside Organizations

SCOAP Award

28.71 In December 1988, the Society of Canadian Office Automation Professionals (SCOAP) selected the Office of the Auditor General to receive its annual Award of Excellence. The award is given each year to the organization that is judged to have demonstrated unusual leadership and innovation in the application of information technology. Organizations nominated for the award come from both the public and private sector.

28.72 SCOAP selected the Office for this award in recognition of the Audit Development in Automated Processing Technology (ADAPT) project, which culminated in the implementation of the "electronic audit briefcase". Almost all of the Office's auditors now use laptop computers for a range of audit tasks. In presenting the Office with the award, the Society particularly noted the Auditor General's personal interest in and commitment to ensuring that his staff are at the forefront in using technology to make themselves more productive. The involvement of the chief executive officer was cited as a critical factor of success in office automation projects.

Elmer B. Staats Award

28.73 The International Organization of Supreme Audit Institutions (INTOSAI) chose an article written by Office staff for the Elmer B. Staats Award. This award, named after the former Comptroller General of the United States in recognition of his many and sustained contributions to INTOSAI, is awarded every three years for the best full-length article appearing during that interval in INTOSAI's quarterly publication, The International Journal of Government Auditing.

28.74 The winning article, entitled "Methodology for Auditing Cost-Recoverable Programs: Theory and Practice", was published in the January 1988 issue. It was co-authored by Principal Vinod Sahgal, Director Neil Maxwell and former Principal David Lewis.

28.75 The Auditor General accepted the award on behalf of its authors at the INTOSAI Congress in Berlin in June.

The Activities of the Working Group on Employment Equity

28.76 The Working Group on Employment Equity addresses equality of access to employment in the Office for women, aboriginal people, visible minorities and handicapped persons.

28.77 The Group has adopted the federal government's employment equity targets and surpassed them in most occupational groupings, for handicapped persons, women and visible minorities. Opportunities remain to improve representation of aboriginal people in most occupational categories and of women in managerial ranks.

The Office won the SCOAP Award of Excellence in recognition of the Audit Development in Automated Processing Technology (ADAPT) project (see paragraphs 28.71 and 28.72).

The Office is Implementing a Stress Control Program

28.78 The Executive Committee decided to implement a stress control program for all staff in the Office of the Auditor General during 1989. The goal of the program is to ensure that stress and energy remain at productive, satisfying, and healthy levels. All employees are participating in the program, which includes a confidential questionnaire on stress, with an interpretation of the results provided to the individual employee, and a 10-hour course on stress management. For managers, an additional day-long session is provided which focusses on the skills managers should be exercising on an ongoing basis to ensure the most productive levels of employee stress, work commitment and satisfaction.

The Office's Program Evaluation and Internal Audit Activities

28.79 The Program Evaluation and Internal Audit (PEIA) group has three principal objectives -- to assess:

- through program evaluation, the effectiveness of the Office's audit activities in support of the scrutiny role of the House of Commons;
- through post-audit quality review, whether the Office selects only matters of significance for audit and audits these in a professional and cost-effective manner;
- through internal audit, whether management practices and procedures throughout the Office reflect due regard for value for money.

Program Evaluation

28.80 A Survey of Chairmen of Departments of Accounting and Directors of Schools of Public Administration in all universities across Canada was carried out during the year. The

The Elmer B. Staats Award was awarded for an article entitled "Methodology for Auditing Cost-Recoverable Programs : Theory and Practice" (see paragraphs 28.73 to 28.75).

objectives of the study were to find out how academics view and rate the work of the Office of the Auditor General; to ascertain whether OAG documents and publications are used in their teaching and research; and to obtain information on student awareness of career opportunities with the OAG.

28.81 The survey concluded that more professors of public administration than accounting use OAG documents and publications in their teaching and research; academics have a high regard for the work of the OAG and rate its work as very important; students in schools of public administration are more aware of career opportunities in the OAG than are students in departments of accounting.

28.82 Recommendations relating to these findings were submitted to the Executive Committee.

28.83 A project to interview a cross-section of users of the annual report was reconsidered. It was decided to change the approach of the study from that outlined in the 1988 report. This will involve exploring alternative formats for graphics and text which would make the report easier to read. These formats will be presented to report users for their comments and suggestions on how the Office can enhance the report's readability.

Post-Audit Quality Review (PAQR)

28.84 Post-audit quality reviews occur annually on a sample of the Office's audit work.

Departmental comprehensive audits

28.85 Two important aspects of comprehensive audits were reviewed this past year in two separate studies:

- the extent to which the Office is relying on the work of internal audit groups in "client" departments; and

- the sufficiency of evidence in support of findings in value-for-money audits.

28.86 Some approaches to value-for-money auditing lend themselves to reliance on internal audit, while others do not. The study on internal audit concluded that value-for-money audits complied with Office standards for reliance. It was recommended that, while the Office should continue to allow flexibility, it should require accountability for a decision to rely on internal audit, based on clarified standards and guidelines.

28.87 The study on sufficiency of evidence found that value-for-money audit findings are generally well supported by evidence. Recommendations were made to strengthen audit sampling procedures and analysis of causes of identified weaknesses in audited organizations, and to address the formulation of recommendations to deal with those causes.

Crown corporations, other entities and the Public Accounts of Canada

28.88 In 1988-89, the PEIA Group reviewed the financial statement audits of five Crown corporations and other entities and eight Public Accounts audits. The review noted that the audits complied with generally accepted auditing standards and with Office standards. Follow-up of earlier PAQR reports showed that most of the PEIA's recommendations had been carried out.

28.89 PEIA paid particular attention to cases where audit teams used innovative cost-saving techniques. Fixed-price contracting of entire audits to public accounting firms seemed to be the most cost effective technique. The long-term policy of the Office on fixed-price contracting is being reviewed.

28.90 In 1989-90, the PEIA Group will begin PAQR work on the special examinations the Office has done on various Crown corporations.

Internal Audit

28.91 The Group did a survey this past year of the Professional Services Branch to identify potential value-for-money issues.

The Office's Contributions to the International Scene

28.92 The Office is considered a world leader in comprehensive auditing, legislative auditing and computer-assisted auditing. Consequently, it is often asked to share its expertise with other countries, especially those seeking to increase their competence in government auditing. This past year the Office was involved in four major international projects.

The International Audit Office Assistance Program

28.93 A fellowship program was implemented in 1980, funded by the Canadian International Development Agency and administered by the Office of the Auditor General and the Canadian Comprehensive Auditing Foundation, to bring senior auditors from developing countries to work and study in the Office of the Auditor General.

28.94 Fellows in 1988-89 were from Chile, China, India, Jordan, Kenya, Papua New Guinea, Senegal, Thailand, Trinidad and Tunisia.

A fellowship program brings senior auditors from developing countries to work and study in the Office (see paragraphs 28.93 to 28.95).

28.95 The Fellows spend one year with the OAG, assisting in a variety of audits and enhancing their knowledge and understanding of public sector accounting and auditing, especially in the area of value for money. As well as gaining practical experience by working with audit teams, they also participate in a number of professional development activities.

The INTOSAI Development Initiative

28.96 At the Twelfth Congress of the International Organization of Supreme Audit Institutions (INTOSAI) in 1986, a proposal to formally establish the INTOSAI Development Initiative (IDI) was adopted.

28.97 The mission of IDI is to foster the advancement of public accounting and auditing, especially in developing nations. This is to be done through information exchange and training for audit practitioners and trainers of Supreme Audit Institutions (SAIs).

28.98 IDI's training program is structured in three parts, based on initial surveys of regional training needs:

- a five-day Human Resource Management seminar for Heads and Deputy Heads of audit institutions, to discuss common regional issues and needs, to develop a regional action plan and to get commitment and support;
- a two-week Training Managers Workshop, aimed at developing a network of individuals capable of organizing and managing the training function of audit institutions and of supporting regional training activities; and
- technical workshops on audit subjects selected through consultations with each region on its needs.

28.99 Since the 1988 Report, IDI has accomplished the following: the Human Resource Management seminar was presented in Peru for Latin America; Training Managers Workshops were conducted in Tunisia and India; and an Audit Workshop for the

Part of IDI's training program includes a two-week Training Managers Workshop, aimed at developing individuals capable of organizing and managing the training function (see paragraph 28.98).

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francophone AFROSAI SAIs was developed jointly with the French, Tunisian and Ivory Coast SAIs. OAG staff participated in the design and delivery of all these training activities.

28.100 IDI was originally set up for a three-year period, with a provision for extending that period based on an assessment of the program's results. At the Thirteenth INTOSAI Congress held in Berlin in June 1989, member SAIs praised the success of IDI and approved its continuation under the same philosophy and approach to the development and delivery of its programs. It also approved the continued location of the IDI Secretariat in the Office of the Auditor General of Canada for the next three years. The Auditor General of Canada is the President of the Board; Deputy Auditor General Edward Rowe is Secretary-Treasurer; and Assistant Auditor General Yvan Gaudette is Executive Vice-President.

28.101 Funding for IDI is currently provided by CIDA, the United Nations Development Program, the Royal Norwegian Ministry of Development Co-operation, the Finnish International Development Agency, the Asian Development Bank, the Caribbean Development Bank and the Commonwealth Secretariat. Discussions on funding are also taking place with the Inter-American Development Bank, the Danish International Development Agency, and the Foreign Ministry of the Netherlands.

Sino-Canadian Auditor Training Project

28.102 Since 1982, the Office of the Auditor General has been involved in an international effort, first with the United Nations and then with the Canadian International Development Agency (CIDA), to assist the People's Republic of China in developing the legislative audit function required by its new constitution.

28.103 The objectives of the first phase of the project were to train Chinese auditors in the concepts, methods and skills practiced in Canada and to train a core of audit instructors for the Audit Administration of the People's Republic of China (AAPRC).

28.104 The first phase of the project was completed within budget in December 1988. All major planned outputs were achieved. The OAG, as an agent of the Canadian International Development Agency (CIDA), provided the necessary professional, technical, and administrative support to meet the project objectives. Both the Canadian and Chinese governments viewed the first phase as a success and a request for a second phase was made by the Chinese government. As a result, the Office of the Auditor General was requested by CIDA to conduct a Project Definition Mission to explore the feasibility of a second phase. A Mission report was presented to CIDA in February 1989 and a proposal was made to continue the project.

28.105 In June 1989 the Minister of External Affairs cancelled proposed funding for the second phase as a result of events in China.

Review of the NATO Audit System

28.106 The Office of the Auditor General has been a key player in a major review of the North Atlantic Treaty Organization (NATO) Audit System. Together with representatives from the audit offices of West Germany, the United Kingdom, the United States, Norway, Italy, Belgium, Denmark, and the Netherlands, Deputy Auditor General Edward Rowe and Principal Vinod Sahgal participated in the Study Group set up by NATO's Working Group on the Reorganization of the NATO Audit System (AC/166). The Working Group was tasked to consult with the NATO Board of Auditors and identify specific improvements to the NATO Audit System. The Group completed its work in the spring of 1989. It made 10 key recommendations that require action by the NATO Council and 10 recommendations that can be acted upon immediately by the International Board of Auditors. A report to the North Atlantic Council has been prepared and discussed with the Chairman of the AC/166, and will likely have been submitted by the publication date of this annual report.

28.107 The overall conclusion of the Group was that if the recommendations in the report are implemented quickly by Council and the Board, there will be a significant improvement in the continuity, efficiency, and effectiveness of the Board. Specific recommendations deal with a variety of topics such as: continuity of the Board members including the length of the Chairman's term of appointment; importance of Board members performing their duties on a full-time basis as required by the audit charter; need for an evaluation of the Board structure and its working arrangements after a trial period following the report of the Group to Council; importance of timely reporting by the Board and the need for quick response by audited bodies to the recommendations of the Board; improved planning of the Board's activities; more aggressive follow-up of previous recommendations made by the Board; and the need to invite the national audit bodies of member countries to participate actively in an informal advisory panel to meet at least twice a year to advise and assist the Board in establishing priorities, methodology, standards, practices and reporting formats.

28.108 Principal Alvin Dickens is currently chairman of the NATO Board of Auditors and three Office staff members have also been seconded to the Board.

Costs Incurred in Preparing Reports on Audits and Special Examinations in Crown Corporations

28.109 Section 147(2) of Part X of the Financial Administration Act (FAA) requires that, where the Auditor General of Canada is the auditor or examiner of a Crown corporation, the costs incurred in preparing any report under Sections 132, 139, 140 and 141 shall be disclosed in his next annual report and be paid out of the moneys appropriated for his Office.

28.110 The costs reported here pursuant to Section 147(2) represent the full costs incurred by the Office in completing the audit and special examination work and preparing particular reports under Sections 132, 139, 140 or 141 of the FAA. These costs are reported here only when the work has been completed. Costs incurred on work not specifically required under Sections 132, 139, 140 or 141, for example, work in relation to issuing prospectuses, advising on information and internal control systems, and helping to resolve accounting issues, are not reported in this chapter.

Annual Audits

28.111 Under Section 132 of the FAA, annual audit reports are required on each parent Crown corporation and its wholly-owned subsidiaries, on their financial statements and on any quantitative information directed by the Treasury Board to be audited. The auditor must also prepare such other reports as the Governor in Council may require.

28.112 Exhibit 28.4 shows the costs incurred in completing the audits and preparing the annual auditor's reports required by Section 132, for those corporations and subsidiaries audited solely or jointly by the Auditor General of Canada. The costs refer to the completed annual audits for fiscal years ending on or before 31 March 1989.

28.113 The costs reported do not include any costs for the audit of quantitative performance information, because no such audits have been requested by the Treasury Board for any of the corporations the Office audited. Similarly, there were no other reports required by the Governor in Council under Section 132.

The work of the Office goes beyond the audits of federal government departments. Activities and technology that support the auditors and their work, evaluation of audits and the Office's productivity, assistance on the international scene -- all are significant Office initiatives.

Special Examinations

28.114 Section 138 of the Financial Administration Act requires each parent Crown corporation named in Schedule III of the Act to cause a special examination to be carried out in respect of itself and, if applicable, its wholly-owned subsidiaries, at least once every five years. The legislation came into effect on 1 September 1984, with the first cycle of special examinations to be completed by 1 September this year. These examinations are separate from the annual audits referred to above and shown in Exhibit 28.4.

28.115 The aim of these examinations is to determine whether, in the period under review, the financial and management control and information systems and management practices of the corporation were maintained in a manner providing reasonable assurance that:

- assets were safeguarded and controlled;
- financial, human and physical resources were managed economically and efficiently; and
- operations were carried out effectively.

28.116 At the completion of a special examination, a report on the findings is submitted to the board of directors of the corporation. For corporations named in Part 1 of Schedule III, or their wholly-owned subsidiaries, the legislation provides for the examiner to draw any necessary matters to Parliament's attention.

28.117 Where, in the examiner's opinion, the special examination report contains information that should be brought to the attention of Parliament, the examiner must, after

COSTS OF PREPARING ANNUAL AUDIT REPORTS FOR FISCAL YEARS ENDING ON OR BEFORE 31 MARCH 1989

Crown Corporation	Fiscal Year Ended	Cost Incurred
Atlantic Pilotage Authority	31.12.88	$ 50,900
Atomic Energy of Canada Limited	31.03.89	378,400
Canada Deposit Insurance Corporation	31.12.88	229,600
Canada Development Investment Corporation (Joint Auditor)	31.12.88	23,700
Cartierville Financial Corporation Inc.	31.12.88	1,600
Canada Harbour Place Corporation	31.03.89	42,500
Canada Lands Company Limited	31.03.89	9,400
Canada Lands Company (Le Vieux-Port de Montréal) Limited	31.03.89	62,100
Canada Lands Company (Mirabel) Limited	31.03.89	46,900
Canada Lands Company (Vieux-Port de Québec) Inc.	31.03.89	11,900
Canada Museums Construction Corporation Inc.	31.03.89	68,300
Canada Post Corporation (Joint Auditor)	31.03.89	313,600
Canadian Commercial Corporation	31.03.89	201,300
Canadian Dairy Commission	31.07.88	204,400
Canadian Livestock Feed Board	31.03.89	47,300
Canadian National (West Indies) Steamships Limited	31.12.88	6,800
Canadian Patents and Development Limited	31.03.89	26,200
Canadian Saltfish Corporation	31.03.89	115,400
Defence Construction (1951) Limited	31.03.89	78,100
Export Development Corporation	31.12.88	640,000
Farm Credit Corporation	31.03.89	294,600
Freshwater Fish Marketing Corporation	30.04.88	136,900
Great Lakes Pilotage Authority, Ltd.	31.12.88	43,400
Harbourfront Corporation	31.03.89	49,100
International Centre for Ocean Development	31.03.89	60,400
Laurentian Pilotage Authority	31.12.88	102,000
National Capital Commission	31.03.89	209,100
Pacific Pilotage Authority	31.12.88	43,000
Royal Canadian Mint	31.12.88	337,100
The St. Lawrence Seaway Authority	31.03.89	112,400
Seaway International Bridge Corporation Ltd	31.12.88	20,900
The Jacques Cartier and Champlain Bridges Incorporated	31.03.89	76,000
Standards Council of Canada	31.03.89	33,500
Teleglobe Canada	31.12.88	25,200

Exhibit 28.4

consulting the board of directors and the appropriate minister, prepare a report on the information for inclusion in the corporation's next annual report. Where an auditor other than the Auditor General of Canada is the examiner, he or she must also consult with the Auditor General and furnish him with a copy of the report on these matters.

28.118 In 1988-89, five special examinations were completed. The costs of these examinations were:

Atlantic Pilotage Authority	$ 145,600
Atomic Energy of Canada Limited	1,060,400
Canadian Commercial Corporation	324,500
Canadian Livestock Feedboard	139,500
Pacific Pilotage Authority	167,500

28.119 There were also 16 special examinations in progress in Crown corporations audited by this Office. Costs of these will be reported in future years, as they are completed.

Office Staff's Contribution to Professional Organizations

28.120 Staff of the Office of the Auditor General invest considerable time, energy and talent in the work of various professional organizations. Their contributions include serving as members on committees and task forces, occupying executive positions, teaching and developing examinations. A list of organizations and the roles played by staff follows. Organizations and staff involvement mentioned elsewhere in this chapter are excluded.

- International Federation of Accountants - Chairman, Public Sector Committee.
- Canadian Comprehensive Auditing Foundation - Vice-Chairman; Member, Board of Governors; Member, Legislative Audit Committee; Member, Reporting Research Steering Group Committee; Member, International Committee.
- Canadian Institute of Chartered Accountants - Member, Board of Governors; Chairman and Associate, Public Sector Accounting & Auditing Committee; Chairman, Physical Assets Study; Member, Professional Development Directors Advisory Committee.
- Institute of Chartered Accountants of British Columbia - First Vice-President.
- Ontario Institute of Chartered Accountants - Member, Council.
- Interprovincial Committee of Chartered Accountants to Harmonize Rules of Professional Conduct - Member.
- Ordre des comptables agréés du Québec - Member, Council; Member, Disciplinary, Comprehensive Auditing and Provincial Legislation Committees; Member, Committee of Members in Business, Government and Industry.
- Certified General Accountants Association of Canada - Member, Task Force on Comprehensive Auditing; Chairman, Primary Committee of the Final Examination for CGA; Examination Developer for CGA's Final Auditing Examination; Reviewer and Developer, Management Auditing Course; Instructor, CGA courses; Member, Management Practices Committee; Member, 1990 CGA Provincial Conference Organization Committee.

- Certified General Accountants Association of Ontario - Member, Board of Governors: Chairman, Chapter Committee; Member, Committee on Public Practice Rights; Member, Planning Committee.

- Society of Management Accountants of Canada - Member, Value for Money Management Committee.

- Financial Management Institute of Canada - Member, Board of Directors, National Chapter; Program Adviser, Professional Development Week; President, Vancouver Chapter; Treasurer, Winnipeg Chapter.

- Institute of Internal Auditors - Vice-President, Vancouver Chapter; Treasurer, Ottawa Chapter; Member, Program Committee.

- Institute of Internal Auditors Research Foundation - Member, Board of Research Advisers.

- EDP Auditors' Association - Treasurer, Vancouver Chapter; Treasurer, Ottawa Chapter;

- Canadian Evaluation Society - Treasurer; Chairman, Administrative Committee; Panel Moderator, 1989 Annual Conference; President, National Capital Chapter; Chairman, Program Committee; Member, Board of Directors, National Capital Chairman; Member, Standards Committee.

- Management Institute of Canada - Program Adviser, Professional Development Week.

- Ottawa Chartered Accountants Association - Member, Executive Committee.

- Canadian Centre for Management Development - Faculty Member and Special Adviser.

- Planning Forum - Director.

- Canadian Study of Parliament Group - Treasurer.

- UNESCO Conference - Delegate.

- Interamerican Accounting Association - Member.

- Canadian Association of Logistics Management - Member.

Advisers to the Auditor General

Membership of the Panel of Senior Advisers

Kenneth G. Belbeck, F.M.C.
Peat Marwick Stevenson & Kellogg

Marcel Caron, F.C.A.
La Presse Ltée

Ralph W. Karthein, C.A.
IBM Canada Ltd.

Giles R. Meikle, F.C.A.
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Gordon H. Cowperthwaite, F.C.A.
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Keith G. Dalglish, F.C.A.
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Alan J. Dilworth, F.C.A.
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William A. Farlinger, F.C.A.
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Edward W. Netten, F.C.A.
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Kenneth R. Stevenson, F.C.A.
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Membership of the Independent Advisory Committee to the Auditor General on Government Accounting and Auditing Standards

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John J. Kelly, C.A.
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Office of the Auditor General of
Canada

Leonard Rutman, Ph.D
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William R. Sloan, F.C.A.
Arthur Andersen & Co.

George F. Windsor, B.Eng., LL.B.,
Osler, Hoskin & Harcourt

APPENDIX A

AUDITOR GENERAL ACT

R.S., c. A-17

An Act respecting the office of the Auditor
General of Canada and matters related
or incidental thereto

SHORT TITLE

Short title

1. This Act may be cited as the *Auditor General Act*. 1976-77, c. 34, s.1.

INTERPRETATION

Definitions

2. In this Act,

"Auditor General"

"Auditor General" means the Auditor General of Canada appointed pursuant to subsection 3(1);

"Crown corporation"

"Crown corporation" has the meaning assigned by section 83 of the *Financial Administration Act;*

"Department"

"department" has the meaning assigned to that term by section 2 of the *Financial Administration Act;*

"Registrar"

"registrar" means the Bank of Canada and a registrar appointed under Part IV of the *Financial Administration Act*. 1976-77, c. 34, s 2, 1984, c. 31, s.14.

AUDITOR GENERAL OF CANADA

Appointment and tenure of office

3. (1) The Governor in Council shall, by commission under the Great Seal, appoint a qualified auditor to be the officer called the Auditor General of Canada to hold office during good behaviour for a term of ten years, but the Auditor General may be removed by the Governor in Council on address of the Senate and House of Commons.

Idem

(2) Notwithstanding subsection (1), the Auditor General ceases to hold office on attaining the age of sixty-five years.

Re-appointment

(3) Once having served as the Auditor General, a person is not eligible for re-appointment to that office.

Vacancy

(4) In the event of the absence or incapacity of the Auditor General or if the office of Auditor General is vacant, the Governor in Council may appoint a person temporarily to perform the duties of Auditor General. 1976-77, c. 34, s.3.

Salary

4. (1) The Auditor General shall be paid a salary equal to the salary of a puisne judge of the Supreme Court of Canada.

Pension benefits

(2) The provisions of the *Public Service Superannuation Act*, other than those relating to tenure of office, apply to the Auditor General except that a person appointed as Auditor General from outside the Public Service may, by notice in writing given to the

President of the Treasury Board not more than sixty days after the date of his appointment as Auditor General, elect to participate in the pension plan provided for in the *Diplomatic Service (Special) Superannuation Act* in which case the provisions of that Act, other than those relating to tenure of office, apply to him and the provisions of the *Public Service Superannuation Act* do not apply to him. 1976-77, c. 34, s.4; 1980-81-82-33, c. 50 s.23, c. 55, s.1.

DUTIES

Examination

5. The Auditor General is the auditor of the accounts of Canada, including those relating to the Consolidated Revenue Fund and as such shall make such examinations and inquiries as he considers necessary to enable him to report as required by this Act. 1976-77, c. 34, s.5.

Idem

6. The Auditor General shall examine the several financial statements required by section 64 of the *Financial Administration Act* to be included in the Public Accounts, and any other statement that the President of the Treasury Board or the Minister of Finance may present for audit and shall express his opinion as to whether they present fairly information in accordance with stated accounting policies of the federal government and on a basis consistent with that of the preceding year together with any reservations he may have. 1976-77, c. 34, s. 6; 1980-81-82-83, c. 170, s. 25.

Report to House of Commons

7. (1) The Auditor General shall report annually to the House of Commons
(a) on the work of his office; and,
(b) on whether, in carrying on the work of his office, he received all the information and explanations he required.

Idem

(2) Each report of the Auditor General under subsection (1) shall call attention to anything that he considers to be of significance and of a nature that should be brought to the attention of the House of Commons, including any cases in which he has observed that

(a) accounts have not been faithfully and properly maintained or public money has not been fully accounted for or paid, where so required by law, into the Consolidated Revenue Fund;

(b) essential records have not been maintained or the rules and procedures applied have been insufficient to safeguard and control public property, to secure an effective check on the assessment, collection and proper allocation of the revenue and to ensure that expenditures have been made only as authorized;

(c) money has been expended other than for purposes for which it was appropriated by Parliament;

(d) money has been expended without due regard to economy or efficiency; or

(e) satisfactory procedures have not been established to measure and report the effectiveness of programs, where such procedures could appropriately and reasonably be implemented.

Submission of report to Speaker and tabling in the House of Commons

(3) Each annual report by the Auditor General to the House of Commons shall be submitted to the Speaker of the House of Commons on or before the 31st day of December in the year to which the report relates and the Speaker of the House of Commons shall lay each such report before the House of Commons forthwith after receipt thereof by him or, if that House is not then sitting, on the first day next thereafter that the House of Commons is sitting. 1976-77, c. 34, s.7.

Special report

8. (1) The Auditor General may make a special report to the House of Commons on any matter of pressing importance or urgency that, in his opinion, should not be deferred until the presentation of his annual report.

Submission of reports to Speaker and tabling in the House of Commons

(2) Each special report of the Auditor General to the House of Commons made under subsection (1) or 19(2) shall be submitted to the Speaker of the House of Commons and shall be laid before the House of Commons by the Speaker of the House of Commons forthwith after receipt thereof by him, or if that House is not then sitting, on the first day next thereafter that the House of Commons is sitting. 1976-77, c. 34, s.8.

Idem

9. The Auditor General shall

(a) make such examination of the accounts and records of each registrar as he deems necessary, and such other examinations of a registrar's transactions as the Minister of Finance may require, and;

(b) when and to the extent required by the Minister of Finance, participate in the destruction of any redeemed or cancelled securities or unissued reserves of securities authorized to be destroyed under the *Financial Administration Act;*

and he may, by arrangement with a registrar, maintain custody and control, jointly with that registrar, of cancelled and unissued securities. 1976-77, c. 34, s.9.

Improper retention of public money

10. Whenever it appears to the Auditor General that any public money has been improperly retained by any person, he shall forthwith report the circumstances of the case to the President of the Treasury Board. 1976-77, c. 34, s.10.

Inquiry and Report

11. The Auditor General may, if in his opinion such an assignment does not interfere with his primary responsibilities, whenever the Governor in Council so requests, inquire into and report on any matter relating to the financial affairs of Canada or to public property or inquire into and report on any person or organization that has received financial aid from the Government of Canada or in respect of which financial aid from the Government of Canada is sought. 1976-77, c. 34, s.11.

Advisory powers

12. The Auditor General may advise appropriate officers and employees in the public service of Canada of matters discovered in his examinations and, in particular, may draw any such matter to the attention of officers and employees engaged in the conduct of the business of the Treasury Board. 1976-77, c. 34, s.12.

ACCESS TO INFORMATION

Access to information

13. (1) Except as provided by any other Act of Parliament that expressly refers to this subsection, the Auditor General is entitled to free access at all convenient times to information that relates to the fulfilment of his responsibilities and he is also entitled to require and receive from members of the public service of Canada such information, reports and explanations as he deems necessary for that purpose.

Stationing of officers in departments

(2) In order to carry out his duties more effectively, the Auditor General may station in any department any person employed in his office, and the department shall provide the necessary office accommodation for any person so stationed.

Oath of secrecy

(3) The Auditor General shall require every person employed in his office who is to examine the accounts of a department or of a Crown corporation pursuant to this Act to comply with any security requirements applicable to, and to take any oath of secrecy required to be taken by, persons employed in that department or Crown corporation.

Inquiries

(4) The Auditor General may examine any person on oath on any matter pertaining to any account subject to audit by him and for the purposes of any such examination the Auditor General may exercise all the powers of a commissioner under Part I of the *Inquiries Act*. 1976-77, c. 34, s.13.

Reliance on audit reports of Crown corporations

14. (1) Notwithstanding subsections (2) and (3), in order to fulfil his responsibilities as the auditor of the accounts of Canada, the Auditor General may rely on the report of the duly appointed auditor of a Crown corporation or of any subsidiary of a Crown corporation.

Auditor General may request information

(2) The Auditor General may request a Crown corporation to obtain and furnish to him such information and explanations from its present or former directors, officers, employees, agents and auditors or those of any of its subsidiaries as are, in his opinion, necessary to enable him to fulfil his responsibilities as the auditor of the accounts of Canada.

Direction of the Governor in Council

(3) If, in the opinion of the Auditor General, a Crown corporation, in response to a request made under subsection (2), fails to provide any or sufficient information or explanations, he may so advise the Governor in Council, who may thereupon direct the officers of the corporation to furnish the Auditor General with such information and explanations and to give him access to those records, documents, books, accounts and vouchers of the corporation or any of its subsidiaries access to which is, in the opinion of the Auditor General, necessary for him to fulfil his responsibilities as the auditor of the accounts of Canada. 1976-77, c. 34, s.14.

STAFF OF THE AUDITOR GENERAL

Officers, etc.

15. (1) Such officers and employees as are necessary to enable the Auditor General to perform his duties shall be appointed in accordance with the *Public Service Employment Act*.

Contract for professional services

(2) Subject to any other Act of Parliament or regulations made thereunder, but without the approval of the Treasury Board, the Auditor General may, within the total dollar limitations established for his office in appropriation Acts, contract for professional services.

Delegation to Auditor General

(3) The Auditor General may exercise and perform, in such manner and subject to such terms and conditions as the Public Service Commission directs, the powers, duties and functions of the Public Service Commission under the *Public Service Employment Act*, other than the powers, duties and functions of the Commission in relation to appeals under sections 21 and 31 of that Act and inquiries under section 34 of that Act.

Suspension

(4) The Auditor General may suspend from the performance of his duty any person employed in his office. 1976-77, c. 34, s.15.

Responsibility for personnel management

16. In respect of persons employed in his office, the Auditor General is authorized to exercise the powers and perform the duties and functions of the Treasury Board under the *Financial Administration Act* that relate to personnel management including the determination of terms and conditions of employment and the responsibility for employer and employee relations, within the meaning of paragraph (1)(e) and sections 11 to 13 of that Act. 1976-77, c. 34, s.16.

Classification standards

17. Classification standards may be prepared for persons employed in the office of the Auditor General to conform with the classifications that the Auditor General recognizes for the purposes of that office. 1976-77, c. 34, s.18.

Delegation

18. The Auditor General may designate a senior member of his staff to sign on his behalf any opinion that he is required to give and any report, other than his annual report on the financial statements of Canada made pursuant to section 64 of the *Financial Administration Act* and his reports to the House of Commons under this Act and any member so signing an opinion or report shall indicate beneath his signature his position in the office of the Auditor General and the fact that he is signing on behalf of the Auditor General. 1976-77, c. 34, s.19.

ESTIMATES

Estimates

19. (1) The Auditor General shall annually prepare an estimate of the sums that will be required to be provided by Parliament for the payment of the salaries, allowances and expenses of his office during the next ensuing fiscal year.

Special report

(2) The Auditor General may make a special report to the House of Commons in the event that amounts provided for his office in the estimates submitted to Parliament are, in his opinion, inadequate to enable him to fulfil the responsibilities of his office. 1976-77, c. 34, s.20.

Approbation allotments

20. The provisions of the *Financial Administration Act* with respect to the division of appropriations into allotments do not apply in respect of appropriations for the office of the Auditor General. 1976-77, c. 34, s.21.

AUDIT OF THE OFFICE OF THE AUDITOR GENERAL

Audit of office of the Auditor General

21. (1) A qualified auditor nominated by the Treasury Board shall examine the receipts and disbursements of the office of the Auditor General and shall report annually the outcome of his examinations to the House of Commons.

Submission of reports and tabling

(2) Each report referred to in subsection (1) shall be submitted to the President of the Treasury Board on or before the 31st day of December in the year to which the report relates and the President of the Treasury Board shall lay each such report before the House of Commons within fifteen days after receipt thereof by him or, if that House is not then sitting, on any of the first fifteen days next thereafter that the House of Commons is sitting. 1976-77, c. 34, s.22.

APPENDIX B

FINANCIAL ADMINISTRATION ACT

EXTRACTS FROM PART X

FINANCIAL ADMINISTRATION ACT

R.S., c. F-11

Extracts from Part X

CROWN CORPORATIONS

Financial Management

Books and systems

131. (1) Each parent Crown corporation shall cause

(a) books of account and records in relation thereto to be kept, and

(b) financial and management control and information systems and management practices to be maintained, in respect of itself and each of its wholly-owned subsidiaries, if any.

Idem

(2) The books, records, systems and practices referred to in subsection (1) shall be kept and maintained in such manner as will provide reasonable assurance that

(a) the assets of the corporation and each subsidiary are safeguarded and controlled;

(b) the transactions of the corporation and each subsidiary are in accordance with this Part, the regulations, the charter and by-laws of the corporation or subsidiary and any directive given to the corporation; and

(c) the financial, human and physical resources of the corporation and each subsidiary are managed economically and efficiently and the operations of the corporation and each subsidiary are carried out effectively.

Internal audit

(3) Each parent Crown corporation shall cause internal audits to be conducted, in respect of itself and each of its wholly-owned subsidiaries, if any, to assess compliance with subsections (1) and (2), unless the Governor in Council is of the opinion that the benefits to be derived from those audits do not justify their cost.

Financial statements

(4) Each parent Crown corporation shall cause financial statements to be prepared annually, in respect of itself and its wholly-owned subsidiaries, if any, in accordance with generally accepted accounting principles as supplemented or augmented by regulations made pursuant to subsection (6).

Form of financial statements

(5) The financial statements of a parent Crown corporation and of a wholly-owned subsidiary shall be prepared in a form that clearly sets out information according to the major businesses or activities of the corporation or subsidiary.

Regulations

(6) The Treasury Board may, for the purposes of subsection (4), make regulations respecting financial statements either generally or in respect of any specified parent Crown corporation or any parent Crown corporation of a specified class, but such regulations shall, in respect of the preparation of financial statements, only supplement or augment generally accepted accounting principles. 1984, c. 31, s. 11.

Auditor's Reports

Annual auditor's report

132. (1) Each parent Crown corporation shall cause an annual auditor's report to be prepared, in respect of itself and its wholly-owned subsidiaries, if any, in accordance with the regulations, on

(a) the financial statements referred to in section 131; and

(b) any quantitative information required to be audited pursuant to subsection (5).

Contents

(2) A report under subsection (1) shall be addressed to the appropriate Minister and shall

(a) include separate statements, whether in the auditor's opinion,

(i) the financial statements are presented fairly in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year,

(ii) the quantitative information is accurate in all material respects and, if applicable, was prepared on a basis consistent with that of the preceding year, and

(iii) the transactions of the corporation and of each subsidiary that have come to his notice in the course of the auditor's examination for the report were in accordance with this Part, the regulations, the charter and by-laws of the corporation or subsidiary and any directive given to the corporation; and

(b) call attention to any other matter falling within the scope of the auditor's examination for the report that, in his opinion, should be brought to the attention of Parliament.

Regulations

(3) The Treasury Board may make regulations prescribing the form and manner in which the report referred to in subsection (1) is to be prepared.

Separate reports

(4) Notwithstanding any other provision of this Part, the auditor of a parent Crown corporation may prepare separate annual auditor's reports on the statements referred to in paragraph (1)(a) and on the information referred to in paragraph (1)(b) if, in the auditor's opinion, separate reports would be more appropriate.

Audit of quantitative information

(5) The Treasury Board may require that any quantitative information required to be included in a parent Crown corporation's annual report pursuant to subsection 150(3) be audited.

Other reports

(6) The auditor of a parent Crown corporation shall prepare such other reports respecting the corporation or any wholly-owned subsidiary of the corporation as the Governor in Council may require.

Examination

(7) An auditor shall make such examination as he considers necessary to enable him to prepare a report under subsection (1) or (6).

Reliance on internal audit

(8) An auditor shall, to the extent he considers practicable, rely on any internal audit of the corporation being audited that is conducted pursuant to subsection 131(3). 1984, c. 31, s. 11.

Errors and omissions

133. (1) A director or officer of a Crown corporation shall forthwith notify the auditor and the audit committee of the corporation, if any, of any error or omission of which the director or officer becomes aware in a financial statement that the auditor or a former auditor has reported on or in a report prepared by the auditor or a former auditor pursuant to section 132.

Idem

(2) Where an auditor or former auditor of a Crown corporation is notified or becomes aware of any error or omission in a financial statement that the auditor or former auditor has reported on or in a report prepared by the auditor or former auditor pursuant to section 132, he shall forthwith notify each director of the corporation of the error or omission if he is of the opinion that the error or omission is material.

Correction

(3) Where an auditor or former auditor of a Crown corporation notifies the directors of an error or omission in a financial statement or report pursuant to subsection (2), the corporation shall prepare a revised financial statement or the auditor or former auditor shall issue a correction to the report, as the case may be, and a copy thereof shall be given to the appropriate Minister. 1984, c. 31, s. 11.

Auditors

Appointment of auditor

134. (1) The auditor of a parent Crown corporation shall be appointed annually by the Governor in Council, after the appropriate Minister has consulted the board of directors of the corporation, and may be removed at any time by the Governor in Council, after the appropriate Minister has consulted the board.

Auditor General

(2) On and after January 1, 1989, the Auditor General of Canada shall be appointed by the Governor in Council as the auditor, or a joint auditor, of each parent Crown corporation named in Part I of Schedule III, unless the Auditor General waives the requirement that he be so appointed.

Idem

(3) Subsections (1) and (2) do not apply in respect of any parent Crown corporation the auditor of which is specified by any other Act of Parliament to be the Auditor General of Canada, but the Auditor General is eligible to be appointed the auditor, or a joint auditor, of a parent Crown corporation pursuant to subsection (1) and section 135 does not apply to him.

Exception

(4) Notwithstanding subsection (1), where the report referred to in subsection 132(1) is to be prepared in respect of a wholly-owned subsidiary separately, the board of directors of the parent Crown corporation that wholly owns the subsidiary shall, after consultation with the board of directors of the subsidiary, appoint the auditor of the subsidiary, and subsections (6) and sections 135 to 137 apply in respect of that auditor as though the references therein to a parent Crown corporation were references to the subsidiary.

Criteria for appointment

(5) The Governor in Council may make regulations prescribing the criteria to be applied in selecting an auditor for appointment pursuant to subsection (1) or (4).

Re-appointment (6) An auditor of a parent Crown corporation is eligible for re-appointment on the expiration of his appointment.

Continuation in office (7) Notwithstanding subsection (1), if an auditor of a parent Crown corporation is not appointed to take office on the expiration of the appointment of an incumbent auditor, the incumbent auditor continues in office until his successor is appointed. 1984, c.31, s.11.

Persons not eligible **135.** (1) A person is disqualified from being appointed or re-appointed or continuing as an auditor of a parent Crown corporation pursuant to section 134 if that person is not independent of the corporation, any of its affiliates, or the directors or officers of the corporation or any of its affiliates.

Independence (2) For the purpose of this section,

(a) independence is a question of fact; and

(b) a person is deemed not to be independent if that person or any of his business partners

(i) is a business partner, director, officer or employee of the parent Crown corporation or any of its affiliates, or a business partner of any director, officer or employee of the corporation or any of its affiliates,

(ii) beneficially owns or controls, directly or indirectly through a trustee, legal representative, agent or other intermediary, a material interest in the shares or debt of the parent Crown corporation or any of its affiliates, or

(iii) has been a receiver, receiver-manager, liquidator or trustee in bankruptcy of the parent Crown corporation or any of its affiliates within two years of his proposed appointment as auditor of the corporation.

Resignation (3) An auditor of a parent Crown corporation who becomes disqualified under this section shall resign forthwith after becoming aware of his disqualification. 1984, c.31, s.11.

Qualifications preserved **136.** Nothing in sections 134 and 135 shall be construed as empowering the appointment, re-appointment or continuation in office as an auditor of a parent Crown corporation of any person who does not meet any qualifications for such appointment, re-appointment or continuation established by any other Act of Parliament. 1984, c. 31, s. 11.

Resignation **137.** A resignation of an auditor of a parent Crown corporation becomes effective at the time the corporation receives a written resignation from the auditor or at the time specified in the resignation, whichever is later. 1984, c. 31, s. 11.

Special Examination

Special examination

138. (1) Each parent Crown corporation shall cause a special examination to be carried out in respect of itself and its wholly owned subsidiaries, if any, to determine if the systems and practices referred to in paragraph 131(1)(b) were, in the period under examination, maintained in a manner that provided reasonable assurance that they met the requirements of paragraphs 131(2)(a) and (c).

Time for examination

(2) A special examination shall be carried out at least once every five years and at such additional times as the Governor in Council, the appropriate Minister or the board of directors of the corporation to be examined may require.

Plan

(3) Before an examiner commences a special examination, he shall survey the systems and practices of the corporation to be examined and submit a plan for the examination, including a statement of the criteria to be applied in the examination, to the audit committee of the corporation, or if there is no audit committee, to the board of directors of the corporation.

Resolution of disagreements

(4) Any disagreement between the examiner and the audit committee or board of directors of a corporation with respect to a plan referred to in subsection (3) may be resolved

(a) in the case of a parent Crown corporation, by the appropriate Minister; and

(b) in the case of a wholly-owned subsidiary, by the parent Crown corporation that wholly owns the subsidiary.

Reliance on internal audit

(5) An examiner shall, to the extent he considers practicable, rely on any internal audit of the corporation being examined conducted pursuant to subsection 131(3). 1984, c.31, s.11.

Report

139. (1) An examiner shall, on completion of the special examination, submit a report on his findings to the board of directors of the corporation examined.

Contents

(2) The report of an examiner under subsection (1) shall include

(a) a statement, whether in the examiner's opinion, with respect to the criteria established pursuant to subsection 138(3), there is reasonable assurance that there are no significant deficiencies in the systems and practices examined; and

(b) a statement of the extent to which the examiner relied on internal audits. 1984, c.31, s.11.

Special report to appropriate Minister

140. Where the examiner of a parent Crown corporation, or a wholly owned subsidiary of a parent Crown corporation, named in Part I of Schedule III is of the opinion that his report under subsection 139(1) contains information that should be brought to the attention of the appropriate Minister, he shall, after consultation with the board of directors of the corporation, or with the board of the subsidiary and corporation, as the case may be, report that information to the Minister and furnish the board or boards with a copy of the report. 1984, c.31, s.11.

Special report to Parliament

141. Where the examiner of a parent Crown corporation, or a wholly-owned subsidiary of a parent Crown corporation, named in Part I of Schedule III of the opinion that his report under subsection 139(1) contains information that should be brought to the attention of Parliament, he shall, after consultation with the appropriate Minister and the board of directors of the corporation, or with the boards of the subsidiary and corporation, as the case may be, prepare a report thereon for inclusion in the next annual report of the corporation and furnish the board or boards, the appropriate Minister and the Auditor General of Canada with copies of the report. 1984, c.31, s.11.

Examiner

142. (1) Subject to subsections (2) and (3), a special examination referred to in section 138 shall be carried out by the auditor of a parent Crown corporation.

Idem

(2) Where, in the opinion of the Governor in Council, a person other than the auditor of a parent Crown corporation should carry out a special examination, the Governor in Council may, after the appropriate Minister has consulted the board of directors of the corporation, appoint an auditor who is qualified for the purpose to carry out the examination in lieu of the auditor of the corporation and may, after the appropriate Minister has consulted the board, remove that qualified auditor at any time.

Exception

(3) Where a special examination is to be carried out in respect of a wholly-owned subsidiary separately, the board of directors of the parent Crown corporation that wholly owns the subsidiary shall, after consultation with the board of directors of the subsidiary, appoint the qualified auditor who is to carry out the special examination.

Applicable provisions

(4) Subject to subsection (5), sections 135 and 137 apply in respect of an examiner as though the references therein to an auditor were references to an examiner.

Auditor General eligible

(5) The Auditor General of Canada is eligible to be appointed an examiner and section 135 does not apply to the Auditor General of Canada in respect of such an appointment. 1984, c. 31, s. 11.

Consultation with Auditor General

Consultation with Auditor General

143. The auditor or examiner of a Crown corporation may at any time consult the Auditor General of Canada on any matter relating to his audit or special examination and shall consult the Auditor General with respect to any matter that, in the opinion of the auditor or examiner, should be brought to the attention of Parliament pursuant to paragraph 132(2)(b) or section 141. 1984, c. 31, s. 11.

Right to Information

Right to information

144. (1) On the demand of the auditor or examiner of a Crown corporation, the present or former directors, officers, employees or agents of the corporation shall furnish such

(a) information and explanations, and

(b) access to records, documents, books, accounts and vouchers of the corporation or any of its subsidiaries as the auditor or examiner considers necessary to enable him to prepare any report as required by this Division and that the directors, officers, employees or agents are reasonably able to furnish.

Idem

(2) On the demand of the auditor or examiner of a Crown corporation, the directors of the corporation shall

(a) obtain from the present or former directors, officers, employees or agents of any subsidiary of the corporation such information and explanations as the auditor or examiner considers necessary to enable him to prepare any report as required by this Division and that the present or former directors, officers, employees or agents are reasonably able to furnish; and

(b) furnish the auditor or examiner with the information and explanations so obtained.

Reliance on reports

(3) An auditor or examiner of a Crown corporation may reasonably rely on any report of any other auditor or examiner. 1984, c. 31, s. 11.

Policy

Restriction

145. Nothing in this Part or the regulations shall be construed as authorizing the auditor or examiner of a Crown corporation to express any opinion on the merits of matters of policy, including the merits of

(a) the objects or purposes for which the corporation is incorporated, or the restrictions on the businesses or activities that it may carry on, as set out in its charter;

(b) the objectives of the corporation; and

(c) any business or policy decision of the corporation or of the Government of Canada. 1984, c. 31, s. 11.

Qualified Privilege

Qualified privilege

146. Any oral or written statement or report made under this Part or the regulations by the auditor or a former auditor, or the examiner or a former examiner, of a parent Crown corporation has qualified privilege. 1984, c. 31, s. 11.

Costs

Cost of audit and examination

147. (1) The amounts paid to an auditor or examiner of a Crown corporation for preparing any report under section 132, 139, 140 or 141 shall be reported to the President of the Treasury Board.

Idem

(2) Where the Auditor General of Canada is the auditor or examiner of a Crown corporation, the costs incurred by him in preparing any report under section 132, 139, 140 or 141 shall be disclosed in the next annual report of the Auditor General and be paid out of the moneys appropriated for his office. 1984, c. 31, s. 11.

Audit Committee

Audit committee

148. (1) Each parent Crown corporation that has four or more directors shall establish an audit committee composed of not less than three directors of the corporation, the majority of whom are not officers or employees of the corporation or any of its affiliates.

Idem

(2) In the case of a parent Crown corporation that has less than four directors, the board of directors of the corporation constitutes the audit committee of the corporation and shall perform the duties and functions assigned to an audit committee by any provision of this Part and the provision shall be construed accordingly.

Duties

(3) The audit committee of a parent Crown corporation shall

(a) review, and advise the board of directors with respect to, the financial statements that are to be included in the annual report of the corporation;

(b) oversee any internal audit of the corporation that is conducted pursuant to subsection 131(3);

(c) review, and advise the board of directors with respect to, the annual auditor's report of the corporation referred to in subsection 132(1);

(d) in the case of a corporation undergoing a special examination, review, and advise the board of directors with respect to, the plan and reports referred to in sections 138 to 141; and

(e) perform such other functions as are assigned to it by the board of directors or the charter or by-laws of the corporation.

Auditor's or examiner's attendance

(4) The auditor and any examiner of a parent Crown corporation are entitled to receive notice of every meeting of the audit committee and, at the expense of the corporation, to attend and be heard at each meeting; and, if so requested by a member of the audit committee, the auditor or examiner shall attend any or every meeting of the committee held during his term of office.

Calling meeting

(5) The auditor or examiner of a parent Crown corporation or a member of the audit committee may call a meeting of the committee.

Wholly-owned subsidiary

(6) Where the report referred to in subsection 132(1) is to be prepared in respect of a wholly-owned subsidiary separately, subsections (1) to (5) apply, with such modifications as the circumstances require, in respect of the subsidiary as though

(a) the references in subsections (1) to (5) to a parent Crown corporation were references to the subsidiary; and

(b) the reference in paragraph (3)(a) to the annual report of the corporation were a reference to the annual report of the parent Crown corporation that wholly owns the subsidiary. 1984, c. 31, s. 11.

Reports

Accounts, etc. to Treasury Board or appropriate Minister

149. (1) A parent Crown corporation shall provide the Treasury Board or the appropriate Minister with such accounts, budgets, returns, statements, documents, records, books, reports or other information as the Board or appropriate Minister may require.

Reports on material developments

(2) The chief executive officer of a parent Crown corporation shall, as soon as reasonably practicable, notify the appropriate Minister, the President of the Treasury Board and any director of the corporation not already aware thereof of any financial or other developments that, in the chief executive officer's opinion, are likely to have a material effect on the performance of the corporation, including its wholly-owned subsidiaries, if any, relative to the corporation's objectives or on the corporation's requirements for funding.

Reports on wholly-owned subsidiaries

(3) Each parent Crown corporation shall forthwith notify the appropriate Minister and the President of the Treasury Board of the name of any corporation that becomes or ceases to be a wholly-owned subsidiary of the corporation. 1984, c. 31, s. 11.

Annual report

150. (1) Each parent Crown corporation shall, as soon as possible, but in any case within three months, after the termination of each financial year submit an annual report on the operations of the corporation in that year concurrently to the appropriate Minister and the President of the Treasury Board, and the appropriate Minister shall cause a copy of the report to be laid before each House of Parliament on any of the first fifteen days on which that House is sitting after he receives it.

Reference to committee

(2) An annual report laid before Parliament pursuant to subsection (1) stands permanently referred to such committee of Parliament as may be designated or established to review matters relating to the business and activities of the corporation submitting the report.

Form and contents

(3) The annual report of a parent Crown corporation shall include

(a) the financial statements of the corporation referred to in section 131,

(b) the annual auditor's report referred to in subsection 132(1),

(c) a statement on the extent to which the corporation has met its objectives for the financial year,

(d) such quantitative information respecting the performance of the corporation, including its wholly-owned subsidiaries, if any, relative to the corporation's objectives as the Treasury Board may require to be included in the annual report, and

(e) such other information as is required by this or any other Act of Parliament, or by the appropriate Minister, the President of the Treasury Board or the Minister of Finance, to be included in the annual report,

and shall be prepared in a form that clearly sets out information according to the major businesses or activities of the corporation and its wholly-owned subsidiaries, if any.

Idem

(4) In addition to any other requirements under this Act or any other Act of Parliament, the Treasury Board may, by regulation, prescribe the information to be included in annual reports and the form in which such information is to be prepared. 1984, c. 31, s. 11.

Annual consolidated report

151. (1) The President of the Treasury Board shall, not later than December 31 of each year, cause a copy of an annual consolidated report on the businesses and activities of all parent Crown corporations for their financial years ending on or before the previous July 31 to be laid before each House of Parliament.

Reference to committee

(2) An annual consolidated report laid before Parliament pursuant to subsection (1) stands permanently referred to such committee of Parliament as may be designated or established to review matters relating to Crown corporations.

Contents

(3) The annual consolidated report referred to in subsection (1) shall include

(a) a list naming, as of a specified date, all Crown corporations and all corporations of which any shares are held by, on behalf of or in trust for the Crown or any Crown corporation;

(b) employment and financial data, including aggregate borrowings of parent Crown corporations; and

(c) such other information as the President of the Treasury Board may determine. 1984, c. 31, s. 11.

Quarterly report

152. (1) The President of the Treasury Board shall cause to be laid before each House of Parliament a copy of a report indicating, in respect of each quarter of each calendar year, the summaries and annual reports that under this Part were to be laid before that House in the quarter, the time at, before or within which they were to be laid and the time they were laid before that House.

Attest

(2) The accuracy of the information contained in each quarterly report shall be attested by the Auditor General of Canada in his annual report to Parliament.

Time for tabling quarterly report

(3) A quarterly report shall be laid before each House of Parliament pursuant to subsection (1) on any of the first thirty days on which that House is sitting after the end of the quarter to which the report relates. 1984, c. 31, s. 11.

APPENDIX C

REPORT ON QUARTERLY REPORTS

REPORT ON THE AUDIT OF QUARTERLY REPORTS ON CROWN CORPORATIONS TABLED BY THE PRESIDENT OF THE TREASURY BOARD

Introduction. The Financial Administration Act requires the President of the Treasury Board to lay quarterly reports before each House of Parliament concerning the timing of tabling, by appropriate ministers, of annual reports and summaries of corporate plans and budgets of Crown corporations subject to the reporting provisions of Part X of the Act.

These quarterly reports allow Parliament to hold the appropriate ministers (and, ultimately, the Crown corporations) accountable for providing it, within the relevant statutory deadlines, with information required under the Financial Administration Act. Accordingly, each quarterly report is required to indicate the annual reports and the summaries of corporate plans, capital budgets and operating budgets (and amendments to them) that were to be tabled before each House during the quarter; the time at, before, or within which they were required to be tabled; and the time they were actually tabled.

Scope. I am required by subsection 152(2) of the Financial Administration Act, to attest to the accuracy of the information contained in the quarterly reports on Crown corporations tabled by the President of the Treasury Board. Accordingly, I have examined the quarterly reports for the four quarters indicated below:

	Tabled in Parliament	
Quarter Ended	**House of Commons**	**Senate**
30 June 1988	18 August 1988	30 August 1988
30 September 1988	24 April 1989	2 May 1989
31 December 1988	11 May 1989	15 May 1989
31 March 1989	15 May 1989	16 May 1989

My examination included a review of the systems and procedures used by Treasury Board to monitor the tabling of the summaries and annual reports in each House of Parliament, a verification of the information contained in each of the quarterly reports, and such other tests and procedures as I considered necessary in the circumstances.

Conclusion. I have concluded that the four quarterly reports listed above contain all the required information about the timing of tabling, by the appropriate ministers, of Crown corporations' annual reports and summaries (and amendments to them) of corporate plans, capital budgets and operating budgets, and in my opinion, the information contained in the quarterly reports is accurate in all significant respects.

Kenneth M. Dye, F.C.A.
Auditor General of Canada

OTTAWA, 6 September 1989